MEMORANDUM

August 9, 2019

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: Informational presentation on the proposed Lease Disposition and Development Agreement and form of a ground lease with an initial 50-year term and a 16-year extension option with TZK Broadway, LLC, a California limited liability company (the "Developer" or "TZK") for the lease and development of a 192-room hotel, a dinner-theater, an approximately 14,000 square foot public open space, and ancillary uses on Seawall Lots 323 and 324 and portions of unimproved Vallejo and Davis Street right-of-ways (collectively, the "Site") located on the west side of The Embarcadero at Vallejo Street

DIRECTOR'S RECOMMENDATION: Informational Only; No Action Required

EXECUTIVE SUMMARY

On September 8, 2015, the Port Commission adopted Resolution No. 15-31[1] authorizing Port staff to enter into an Exclusive Negotiation Agreement ("ENA") with TZK for a one-year term with four six-month extension options, among other terms, to complete certain tasks and negotiate terms and conditions for leasing the Site for the development of a 180-200 room hotel, a dinner-theater, a 14,000-square-foot public open space, and ancillary uses (the "Development" or "Project"). The Site shown on **Exhibit "A" Site Map,** is currently used for surface parking. On April 26, 2016, the Port

THIS PRINT COVERS CALENDAR ITEM NO. 11A

[1] See: https://sfport.com/sites/default/files/FileCenter/Documents/10429-Item%2014B-Teatro%20ZinZanni%20ENA%20FINAL%209-2.pdf

Commission adopted Resolution No. 16-18,[2] endorsing a non-binding term sheet ("Term Sheet") of terms and conditions for the Lease Disposition and Development Agreement ("LDDA") and lease ("Lease"). On July 12, 2016, the Board of Supervisors adopted Resolution No. 277-16[3] and also endorsed the Term Sheet. On September 25, 2018, the Port Commission adopted Resolution No. 18-53[4] and authorized the First Amendment to the ENA to provide for two additional six-month extension options if needed by TZK to complete entitlements and lease negotiations for the Development.

Since the September 2018 presentation to the Port Commission, Port staff and TZK have further negotiated the terms and conditions that will be recommended for the LDDA and Lease. This Memorandum provides an update on the Development, the final terms and conditions proposed, and the next steps and expected timeline for the Development.

DEVELOPMENT SUMMARY

The Development is summarized in the table below.

Table 1 - Development Summary

Site Area	59,750 Square Feet
Proposed Building	
Building Height	40 Feet (4 stories) - 55 feet with elevator penthouse
Teatro ZinZanni - Entertainment Venue including Back of House, Circulation and the Spiegeltent:	29,570 Gross Square Feet
Hotel, including Back of House and Circulation:	192 Rooms on three levels, Floors 2, 3, and 4 118,130 Gross Square Feet
Restaurant Food and Beverage:	4,420 Gross Square Feet
Overall Building Gross Floor Area:	147,880 Gross Square Feet

[2] See: https://sfport.com/sites/default/files/Commission/Documents/Commission%20Meeting%20Staff%20Reports/2016%20Commission%20Meeting%20Items/APR26/Item%2012A%20SWL%20324%20Action%20Memo%20for%20042616%20PC%20Meeting.pdf

[3] See: https://www.sfbos.org/ftp/uploadedfiles/bdsupvrs/resolutions16/r0277-16.pdf

[4] See: https://sfport.com/sites/default/files/Commission/Documents/Item%2011A%20SWL%20324%20ENA%20First%20Amendment.05.09142018.pdf

Open Space:	Public Park – 14,000 Square Feet Common – Open Roof Terrace – 3,970 Square Feet
Bicycle Parking Spaces:	20 Class I; 43 Class II
Loading Spaces:	2
Projected Total Development Cost:	$142,000,000
Funding Sources:	Debt: $ 82,000,000 Equity: $ 60,000,000 Total: $142,000,000

The Port's key goal for this Development is the leasing of the Site to achieve multiple strategic objectives as explained later in this Memorandum. Staff anticipates this Development, if approved, will provide multiple benefits to the Port, the community, and the City, including: (a) activation of the Site for its highest and best use with approximately $142 million in estimated private capital investment; (b) a significant contribution to the integrity of Northeast Waterfront Historic District; (c) retention of Teatro ZinZanni, a cultural asset that will draws people to the Waterfront, (d) addition of a new source of revenues for the Harbor Fund, (e) generation of new jobs along the Waterfront , and (f) new tax revenues for the City.

Port's and Developer's representatives have completed negotiations of the terms and conditions for the proposed real estate transaction, for consideration by approving bodies. At the next Port Commission meeting, Port staff intends to request the Port Commission's consideration and approval of the LDDA and Lease. Port staff is making this presentation to allow Port Commission to provide input and feedback to staff and for the public to review and comment on the proposed development and deal structure that will be included in the LDDA and the Lease, the two **key transaction documents** to implement the Development.

The proposed Transaction Documents include:

LDDA (Lease Disposition and Development Agreement) between the Port and TZK. The LDDA's primary purpose is to: (1) set the list of conditions TZK must satisfy before the Port will allow escrow to close and Site possession to transfer to TZK and (2) govern the signatories' rights and obligations through construction of the Development. Conditions to close escrow include: achievement of all regulatory approvals to begin construction; demonstration of sufficient financial resources to commence and complete construction; and posting of construction bonds, among other conditions. Other key terms of the LDDA include: **(a)** a 12-month period to close escrow on the lease (with four three-month extension options with fees, for a total of up to two years), **(b)** requirement that TZK complete construction within 24 months after lease commencement, subject to four, three-month extension options with a $25,000 fee per each three-month extension, **(c)** description of LDDA fees payable to the Port, **(d)** requirement for payment of Port transaction costs, **(e)** Port's standard transaction provisions, including liquidated damages for failure to complete construction on time, insurance, and indemnification, and **(f)** Port's consent for transfers and assignments, among other terms. The LDDA, which terminates once construction is completed, is subject to Port Commission approval only.

Lease (Ground Lease), between the Port and TZK. The Lease's purpose is to convey property rights subject to the negotiated terms and conditions under which the Site is being leased to TZK. Proposed key terms include: **(a)** a 50-year initial term with a 16-year extension option; **(b)** rent to include **(i) Minimum Base Rent** per year for both construction and operation periods; **(ii) Percentage Rent** during the operation period; **(iii) Participation Rent** during operation phase and refinancing and sale events; **(c)** Port's standard lease provisions, including insurance, indemnity, sea level rise and flooding provisions; and **(d)** prior consent for transfers and assignments, among others. The lease is subject to approval by the Port Commission and the Board of Supervisors.

The remainder of this staff report provides background information and discusses the key terms proposed for the Transaction Documents. At the next Port Commission meeting, Port staff intends to request the Port Commission's consideration and approval of the Transaction Documents and the Development's schematic design, adoption of environmental and public trust findings, and authorization for the Executive Director to seek necessary Board of Supervisors' approvals for the Transaction Documents and formation of a sub-project area within the Port's Infrastructure Financing District for the purposes of collecting tax increment from the Site for Port's Capital Plan and/or the Seawall Resiliency Program.

STRATEGIC OBJECTIVE

The Development, if approved and implemented, is expected to contribute in a substantial way to meeting the *livability, sustainability, and economic vitality objectives* of the Port's Strategic Plan.

- *Equity Objective*: The Development will provide business opportunities for local businesses and develop a new live theater space for Teatro ZinZanni's operation. Under the City's music and culture sustainability policy, as articulated in Chapter 90A of the Administrative Code, the City "is committed to supporting and encouraging the use of City and County property, including Port property, for indoor and outdoor music and other cultural events" and is committed to preserving and enhancing San Francisco's music and performance venues from displacement due to development. The Development is expected to contribute to the growth of capital funding for the Port through increased leasing revenues and addition of a subarea to the Port's infrastructure financing district to leverage the available tax increment.

- *Sustainability Objectives*: The Development is expected to incorporate a variety of sustainable practices including environmentally sensitive demolition techniques, recycling of demolition and construction waste, use of recycled

construction materials, installation of high-efficiency building systems and appliances, storm water management, zero waste operations, and green building standards.
- *Stability Objectives*: Adding revenues from a hotel and dinner-theater operations diversifies the Port's asset portfolio and supports the durability of the Port's lease revenue. Changing the Site from its current use as a surface parking lot to its highest and best use[5] will maximize asset value and increase the income stream to the Port from the Site. The Development is expected to increase Port revenues and increase Port's capital budget through the formation of a sub-project area within the Port Infrastructure Financing District.

BACKGROUND

Site Description and Permitted Uses: Seawall Lots ("SWLs") 323 and 324 are two nearly triangular land parcels with a combined surface area of approximately 42,719 square feet with frontages on The Embarcadero, Broadway, Davis, and Vallejo Streets. They are proposed to be developed along with portions of Vallejo and Davis Streets that are also held by the Port and abut the SWLs ("Paper Streets"). SWLs 323 and 324 and the two Paper Streets have a combined land area of approximately 57,170 square feet and form the Site. The Site is currently paved with asphalt, striped for 227 self-parked stalls, and leased on an interim basis to a parking operator, SP Plus-Hide Parking Joint Venture (the "SP+Hide"). The Site generated approximately, $739,309 in fiscal year (FY) 2015-2016, $667,172 in FY 2016-2017 and $968,760 in FY 2017-2018 in net revenues to the Port. Current fiscal year revenues are on track to generate slightly less than the prior year's subject to end of year revenue adjustments.

Hotel, entertainment, theater, retail, and public open space, among others, are listed as acceptable uses for SWLs 323 and 324 in the Port's Waterfront Land Use Plan, the City Planning Department's Northeastern Waterfront Subarea Plan, and the Planning Department's Northeast Embarcadero Study. The Site is located in the Northeast Waterfront Historic District and within a C-2 (Community Business) zoning district and a 40-X Height and Bulk district.

Teatro ZinZanni and Relocation Plan: Teatro ZinZanni is a popular dinner theater performed in a historic Spiegel tent and was a fixture on the San Francisco waterfront for over a decade. The tent provides a big top setting for live music, comedy, and acrobatic entertainment. It is a unique hybrid of comedy, theater, music, and dining that is part circus and part cabaret. It combines improvisational comedy, vaudeville revue, music, dance, and cirque into an engaging performance. It operates venues in Seattle and Chicago and operated a venue in San Francisco until 2011.

Teatro and the Port entered into a lease in 1999 for Teatro to use a portion of Piers 27 and 29 for its dinner theater and cabaret operations (the "Theater Lease"). The Theater

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[5] Highest and best use is defined as the use allowed under current zoning which returns the highest land value.

Lease was amended a number of times; it expired in 2005, and continued on a holdover month-to-month basis until 2011. To accommodate the 34th America's Cup and the construction of the new James R. Herman Cruise Terminal at Pier 27, the Port and Teatro mutually agreed to terminate the Theater Lease and identified a portion of SWL 324 as a potential relocation site. If Teatro satisfied certain pre-conditions (such as project design compatible with the Northeast Waterfront Historic District and completion of environmental review, among others), the parties would enter into a new lease for a portion of SWL 324.

Project Sponsor: Teatro and Kenwood Investments formed TZK to undertake the Development. At approval of the ENA in 2015, TZK was comprised of two-member companies: Kenwood Investments No. 6, LLC, a California limited liability company ("KWI #6") established by Kenwood Investments, and TZZ, LLC, a Washington limited liability company ("TZZ") established by Teatro ZinZanni. In 2018, one of the founding members of TZK informed Port staff that PresidioCo Holdings, LLC ("Presidio") was admitted into TZK's membership. This admission does not constitute a "Transfer" under the ENA that required Port's prior consent. TZK shared with Port staff that it sought to admit Presidio to increase TZK's hotel development capacity and ability to raise additional capital. In particular, the partnership is focused on successfully raising capital for the somewhat unusual combination hotel and dinner theater operating model, securing affiliation with one of the major hospitality brands, reservation systems, and setting minimum management standards to meet capital requirements.

TZK provided Port staff information on Presidio's financial wherewithal and experience, particularly with hotel development capitalization, management, and operation. Presidio is reported to have owned and operated, and continues to own and operate, independent boutique properties, full-service conference center hotels, full-service resort hotels as well as select- and limited-service hospitality properties in different locations across the United States. Presidio has demonstrated that it has both the experience and financial standing to assist TZK in achieving the ultimate goal of a new home for Teatro ZinZanni in San Francisco and a successful hotel on the Site. With Presidio on board, TZK improved the hotel's interior layout to increase efficiency and save costs, identified possible capital sources to invest in the development, and advanced discussions with a franchisor that is expected to be a good fit for this hotel with its unique attributes.

PROJECT COMPONENTS

The Proposed Development: A summary of the Development is provided in Table 1 in the early part of this Memorandum. The three key elements of the development are described below.

1. *The Entertainment Venue*

The entertainment venue is proposed to include approximately 29,570 gross square feet to house the historic Spiegeltent and seating for the venue, kitchen, bar, bathrooms, welcoming areas, ticket booth, merchandise area, shared indoor public space, and back-of-house activities. This venue would be located inside a clear gazebo-like structure, constructed of glass and metal with steel or metal supports, at the northern end of the site adjacent to the public park. The glass gazebo-like structure would be clear to allow pedestrians walking past the structure to view the historic Spiegeltent and see through the backstage area during daylight hours. The structure's roofline would be glass with metal. This venue is expected to accommodate a maximum of 285 patrons and to be in use daily, with live shows performed several times each week from approximately 6:30 pm to midnight, and would have operational staff on site from 8:00 am, for pre-show cleaning, set-up, and other necessary back-of-the house activities, through 2:00 am when the final clean up would be completed

This entertainment venue is planned to include a small outdoor raised stage area located at the south end of the public park, attached to the back-of-house portion of the entertainment venue. Operable doors on the northern side of the entertainment venue structure would open up onto the outdoor stage area. The operable doors would remain closed during regularly scheduled performances. The outdoor raised stage that would be located in the public park could be programmed and used for small-scale community and neighborhood events; small-scale theater performances by local schools and community groups; and other neighborhood events, such as weekly exercise classes or a children's dance or singing performance. The public park is only 14,000 square feet and has limited capacity because of its size, which would restrict the size of events that could take place. Activities that would occur in the public park would allow for passage of pedestrian traffic through the site.

2. *The Hotel*

The hotel component is proposed to include a total of approximately 118,000 gross square feet, of which 14,560 gross square feet would be at ground level for entry and drop-off areas for guests, the front desk, a concierge, gathering space, retail, restaurant or café uses, back-of-house uses, and elevator and stairwell access. The hotel would also include a restaurant and bar. Operating hours for the restaurant or cafe would be approximately 6 a.m. to midnight, 7 days a week. The bar portion of the hotel would be permitted to remain open until 2 a.m., although it is anticipated to close earlier on weekdays. The restaurant and bar are proposed to include an outdoor patio along the eastern side of the building, along The Embarcadero. Above the ground-level floor, the proposed project would include approximately three floors of hotel uses totaling 95,560 gross square feet and 192 hotel guest rooms. The hotel would also include an approximately 3,970 gross square foot rooftop deck, serving food and beverages from the hotel's bar and restaurant or cafe services, for use by hotel guests only. The roof would include screens for screening rooftop mechanical devices from the street and surrounding areas, as well as low-impact-design stormwater facilities and wind-protected outdoor spaces for hotel guests.

3. *The Public Park*

The proposed Development includes an approximately 14,000-gsf public park in the northern portion of the Site parallel to The Embarcadero, as depicted in **Exhibit "B,"** Proposed Project Drawings. The park would consist of both landscaping and hardscape, with benches and lighting in and around the park. The park would include pathways for pedestrian access from The Embarcadero through to Vallejo and Davis streets. The public park would provide space for a variety of informal activities, such as family and community picnics, and gatherings, neighborhood yoga and tai chi classes, programming for toddlers and young children, educational events for elementary school students, and pedestrian strolling, and sitting. The park would also include view mounds to allow visitors to "get up to see the bay," as well as moveable and permanent seating and tables, wayfaring, lighting, historic signage, and public art features. Additionally, the park would include iconic statuary art at the intersection of Davis and Vallejo streets, marking the park as an important destination along the waterfront.

The public park would be used for informal passive activities on weekdays and weekends during normal business hours, subject to lease provision on compliance with the Port's Good Neighbor Standards. The park may also include temporary events, approximately one time per week, under the supervision of the Developer, in accordance with Lease terms[6] and the City's event policies. Activities could involve hosting a food truck gathering, lunchtime music or lecture session, or activities related to local festivals or events in the vicinity or other parts of San Francisco, such as Sunday Streets. The public park may also be used for private events related to the theater or hotel. For example, if a wedding were held at the hotel, guests could enjoy drinks outside before going inside for the celebration. Sound would be amplified only with the appropriate approvals, obtained in advance from the applicable City department(s).

TZK is responsible for maintenance of the park, including trash removal and recycling systems, and security to keep the park clean and safe. A portion of the park area will provide the San Francisco Fire Department with a new emergency-vehicle access point between The Embarcadero and Vallejo Street, which area will be closed to other vehicles with new movable bollards where none exist today.

Vehicle Parking/Loading/Bicycle Parking

The Development is proposed to provide zero off-street vehicle parking onsite. Instead, parking is proposed to be provided through offsite parking and valet services. The proposed valet service would park hotel guests' vehicles at nearby off-street parking facilities. Several existing parking lots and parking structures are located near the Site. TZK is planning to send early and regular communication to patrons to encourage taking public transit, cabs, or ridesharing services to the hotel and entertainment venue and would inform them of the many off-site, self-parking locations close to the theater, such as parking at 847 Front Street, Pier 19, 1000 Front Street, and One Maritime Plaza.

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[6] The Guidelines & Application for Special Events, https://sfport.com/special-events-port, set forth the applicable regulations governing special events at Port property.

A new 80-foot-long curbside passenger loading space ("white curb") along the northern side of Broadway is being proposed to provide ingress and egress into the site for hotel guests, theater guests, and other patrons. The passenger loading space would be located adjacent to the hotel lobby entrance into the building and would be used in a curbside valet operation for hotel guests, theater guests, and other patrons and ride sharing drop-off.

A loading zone for deliveries and services is proposed along the project frontage on the eastern side of Davis Street. The loading dock and service area would be used exclusively for deliveries, service providers including waste collection, and recycling and will include an audible and visual signal to alert pedestrians to truck movement at the dock.

Approximately 63 bicycle parking spaces, consisting of 20 *class I* bicycle parking spaces and 43 *class II* bicycle parking spaces are proposed for the Development. Access to the class I bicycle parking spaces would be via a secured door into the building along Davis Street and are reserved for use by hotel and other employees only.

The estimated Uses and Sources of Funds for the development are provided in Table 2.

Table 2 – Estimated Total Uses and Sources of Funds

Total Uses of Funds	**Amounts**
Land Cost – (With a Ground Lease, there is no upfront land cost)	$0
Total Hard Cost:	$89,000,000
Total Soft Cost:	$53,000,000
Total Development Cost:	**$142,000,000**
Total Sources of Funds:	
Senior Loan + PACE Debt:	$85,500,000
Preferred Equity	$30,000,000
Marriott & Interstate Key Money	$2,500,000
Third Party/Sponsor Equity	$25,000,000
Total Sources of Funds	**$142,000,000**

Updated Development Schematics are attached as **Exhibit "B," Proposed Project Drawings**.

UPDATE ON LAND USE AND REGULATORY APPROVALS

Environmental Review under California Environmental Quality Act
On December 30, 2015, the Developer filed Environmental Review Application for the Development with the City Planning Department. The Planning Department prepared a Draft Initial Study/Preliminary Mitigated Negative Declaration ("IS/PMND") for the Development and published the Draft IS/PMND for public review on October 17, 2018. The IS/PMND was available for public comment until November 19, 2018. No appeal was filed against the IS/PMND and the MND became final on December 21, 2018.

The Planning Commission approved the issuance of the Final Mitigated Negative Declaration ("FMND") as prepared by the Planning Department in compliance with the California Environmental Quality Act ("CEQA", CEQA Guidelines (Title 14 California Code of Regulations Sections 15000 et seq.), and San Francisco Administrative Code Chapter 31 ("Chapter 31").

The Planning Commission, after reviewing and considering the FMND and Initial Study, found that the contents of said report and the procedures through which the FMND and Initial Study were prepared, publicized, and reviewed in compliance with CEQA, the CEQA Guidelines, and Chapter 31 and that the FMND and Initial Study are adequate, accurate and objective, reflect the independent analysis and judgment of the Planning Department and the Planning Commission. Planning Department staff prepared a Mitigation Monitoring and Reporting program ("MMRP"), which was made available to the public and the Planning Director for review, consideration, and action. The MMRP will be incorporated into the Lease.

Architectural and Urban Design Review for Compliance with Historic District
The Project's architecture and urban design have been reviewed by the Architectural Review Committee ("ARC") of the Historic Preservation Commission ("HPC") and the Waterfront Design Advisory Committee ("WDAC") for compatibility with the Historic District and both ARC and WDAC found the overall design acceptable and provided a few comments. On March 6, 2019, HPC adopted Motion No. 0370 finding that the proposed Development is consistent with Article 10 of the Planning Code and the Secretary of the Interior's Standards for Rehabilitation in conformance with the architectural plans filed with the Planning Department subject to the conditions and findings listed in its Motion No. 0370.

Conditional Use Authorization and Street Vacation
On May 2, 2019, the Planning Commission conducted a duly noticed public hearing at a regularly scheduled meeting on Conditional Use Authorization Application and General Plan Referral Nos. 2015-016326 CUA and 2016- 011011GPR and granted a Conditional Use Authorization for the Development pursuant to Planning Code Sections 210.1, 240.3 and 303 to allow a hotel use within the C-2 Zoning District subject to the conditions and findings listed in the Motion No. 20444. It also adopted for the

Development Findings of Consistency with the General Plan for street vacations pursuant to Section 4.105 of the City Charter and Section 2A.53 of Administrative Code.

Current Status of the ENA

ENA Key Requirements and Performance Schedule:
TZK has completed the key tasks it is required to complete under the ENA before seeking approval of the Transaction Documents: it obtained endorsement of Term Sheet by Port and the Board, reviewed the Site's suitability for the proposed Development, conducted community outreach to stakeholders to gather input and keep community members informed, completed environmental review required under CEQA and Chapter 31; and completed architectural and urban design review by the Planning Department, the Waterfront Design Advisory Committee, and the City Historic Preservation Commission which has found the Development's urban and architectural design compatible with the design requirements for the Northeast Historic District. TZK has received the required Conditional Use authorization from the City Planning Commission. TZK is in full compliance with the ENA and the ENA will expire on November 4, 2019.

The Development Provides Numerous Benefits to the Public Trust

The proposed lease furthers and supports the public trust and the Burton Act because it provides numerous public benefits to the public trust, including;

a. new hotel, dinner-theater and other visitor-serving uses that will enhance public use and enjoyment of the waterfront

b. creation of new public open space

c. elimination of barriers to the waterfront and uniting the landside with the waterfront

d. enhanced pedestrian, bicycle and transit access along the Waterfront, and

e. increased rent revenues to the Harbor Fund that will exceed the current and projected revenues from existing parking operations on the Site.

The attached **Exhibit D** includes more details on the benefits the proposed Development is expected to provide the public trust, and how it furthers the purposes of the public trust for commerce, navigation and fisheries.

THE PROPOSED TRANSACTION DOCUMENTS

The transaction documents and its key terms are summarized below. Attached as **Exhibit "C**," is a Summary of the Key Business Terms from the Term Sheet annotated to indicate changes to the terms since endorsement by the Port Commission and the Board of Supervisors.

SUMMARY OF PROPOSED TERMS FOR THE LDDA

The LDDA will provide TZK with a binding agreement confirming the Port's intension to lease the Site to TZK subject to the conditions it must satisfy before the Port will allow escrow to close and Site possession to transfer to TZK. The key terms of the LDDA include:

1. **The Premises or Site to be Leased:** The site to be leased consists of four parcels, SWLs 323 and 324 and the two abutting unimproved portions of right-of-way parcels ("Paper Streets"), with a combined land area of approximately 59,750 square feet and located on the west side of The Embarcadero at Vallejo Street. It will be leased in "As Is" conditions.

2. **Development Program:** This is described earlier in the Staff Report. *TZK has further vetted and updated the Development as of July 2018. Please refer to* **Table 1, Development Summary***, for more detail.*

3. **Estimated Total Development Cost and Sources of Funding**: TZK is responsible for funding the Development estimated to cost approximately $142 million. TZK is required to provide performance and payment bonds for the Development as part of Port's risk mitigation measures. Funding sources are identified in **Table 2, Total Uses and Sources of Funds** in the earlier part of this Memorandum.

4. **Term**: a 12-month term (with four three-month extensions options with fees) to close escrow and have Site possession transferred to TZK.

5. **Time to Complete Construction**: Complete construction within 24 months after lease commencement subject to four three-month extension options with $25,000 fee per extension

6. **Port Transaction Cost:** Pay Port Transaction Cost during the LDDA Period, is capped at $300,000. If the LDDA period is extended because of litigation, the cap will be lifted to cover the more than expected Port cost.

7. **Liquidated Damages:** Pay Liquidated Damages for delay in completing construction on schedule.

8. **Force Majeure**: Force Majeure or time credit for a delay that is beyond TZK's control; the time credit is subject to Port's prior consent. Examples of such delays include an occurrence of earthquake, terrorist act, nonparty litigation, etc. that prevents TZK from performing on time.

9. **Conditions to Close Escrow and Enter into the Lease Include, Among Others:**

    a. TZK must have completed all required predevelopment tasks and is ready to close escrow.

b. Port staff must have reviewed and approved the Developer's financing plan, including lenders' commitment letters, and balanced sources and uses of funds, and simultaneous closing of the construction loan(s).
c. Port must have reviewed and approved the Developer's updated scope of development and construction documents.
d. TZK must have received all required approvals required to start construction.
e. TZK must not be in uncured default under the LDDA.

10. **City and Other Standard Requirements:** The LDDA will include all applicable Port and City requirements (e.g. insurance requirements, non-discrimination requirements, etc.).

11. Key Exhibits to the LDDA:

a. *Scope of Development*. The Scope of Development sets forth the improvements that are to be constructed on the Site by the Developer.
b. *Schedule of Performance*. The Schedule of Performance sets forth the deadlines by which the parties are required to submit or approve documents prior to close of escrow. All deadlines are subject to force majeure.
c. *Schematic Drawings*. Schematic Drawings consisting of site plans and elevations approved by the Port Commission.
d. *Development Budget*. The Development Budget for the Project, showing a total development cost of $142,000,000.
e. *Form of ground lease*. The form of the Lease includes the terms described in the next section.

SUMMARY OF PROPOSED LEASE TERMS

The purpose of the Lease is to set forth all of the terms and conditions on which the Port agrees to lease the Site to TZK and TZK agrees to lease the Site from the Port, including the respective duties and obligations of the Port, as landlord, and TZK, as tenant. The Lease was negotiated based on the Term Sheet endorsed in 2016 by the Port Commission and the Board of Supervisors. Some of the terms of the Term Sheet incorporated into the Lease have been updated by Port staff and TZK representatives to address the current project circumstances and the current market conditions.

Attached as **Exhibit "C,"** is a **Summary of the Key Business Terms from the Term Sheet** annotated to indicate updates to the terms.

1. **The Premises or Site:** Comprised of four parcels, SWLs 323 and 324, and the two Paper Streets, for a combined land area of approximately 59,750 square feet. It will be leased in "As Is" condition.

2. **Development Program:** This is described earlier in the Staff Report. TZK has further vetted and updated the Development as of July 2018. *Please refer to* **Table 1, Development Summary***, for more detail.*

3. **Total Development Cost and Sources of Funding**: TZK is responsible for funding the Development estimated to cost approximately $142 million. TZK is responsible for paying all of the Port's transaction costs and for providing performance and payment bonds for the Development. A Development Budget with projected Total Uses and Sources of the Funds will be attached to the Lease to document the estimated budget, debt and equity amounts.

4. **Complete Construction**: TZK must complete construction within 24 months after lease commencement, subject to four three-month extension options with a $25,000 fee for each extension.

5. **Liquidated Damages for Failure to Timely Complete Construction:** If TZK fails to complete construction within the 36-month period (24-month construction period plus the four three-month extension periods), it must pay the Port $1,350 for each day it has yet to complete construction. This $1,350 per day is based on the average rent per day the Port will lose for the development failing to start operations on schedule.

6. **Lease Term:** 50 years initial term, plus one 16-year extension option. The 16-year extension is subject to TZK remaining as a "tenant in good standing" and having exercised the extension option within two years prior to the end of the initial term. This term is based on the Developer's need to attract required capital investments, amortize the capital investment, and the Port's need to review the lease and development 48 years from lease commencement date based on the then-existing conditions including sea level rise.

7. **Construction Period Rent:** The Minimum Base Rent of $**1,000,000** (escalated from the <u>$890,000</u> set in the Term Sheet) is set for Lease Years 1 and 2, when the development's improvements are being constructed. This minimum base rent is based on maintaining the current stream of income the Port is receiving from the Site while also recognizing that the Developer is not earning any revenue from the development during this period.

8. **Operation Period Rent**: **Minimum Base Rent** <u>plus</u> **Percentage Rent** as defined below**.** The Developer will pay the Port the greater of the Minimum Base Rent or the Percentage Rent. The exact amount of percentage rent due to the Port will be confirmed at the end of the hotel operation's fiscal year when the required supporting financial reports are prepared. The Operation Period Minimum Base Rent has been escalated to account for the passage of time since the Term Sheet was endorsed.

9. **Minimum Base Rent for the first two years of the Operation Period**: The Minimum Base Rent for Lease years 3 and 4 is set at **$1,007,000 per year** (escalated from the <u>$915,000</u> set in the Term Sheet) to allow the operation to address (a) unexpected or greater than expected start-up costs, (b) greater than expected operational expenses, and (c) lower-than-projected revenues because

the new hotel has yet to establish a robust customer base or achieve the requisite market share. If the hotel operations do well by attaining 80% occupancy in either of these two years, TZK will pay the Port the applicable Percentage Rent, currently estimated at between $1.363 million and $1.534 million.

10. **Minimum Base Rent from third through fifth years of Operation Period**: For Lease Years 5 through 7 *(Operation Period Years 3 through 5)*, the Minimum Base Rent starts at **$1,471,000** (escalated from the $1,366,000 set in the Term Sheet) and escalates annually by the annual increase in the Consumer Price Index for the Bay Area ("CPI"), with a minimum increase of 2.5% and a maximum increase of 3.5% annually until reset in the 11th year of the Operation Period. This arrangement sets a floor to protect the minimum base rent the Port will earn from the Site regardless of how the development is performing financially. It also provides protection for the Developer from larger than budgeted rental spikes.

11. **Minimum Base Rent Reset:** At the end of every 10-year interval of the Lease Term Operation Period, (beginning in the 13th Lease Year, Hotel Operation Period Year 11), the Minimum Base Rent will be reset to **the greater** of **(a)** then existing CPI-adjusted Minimum Base Rent and **(b)** 65% of the average of the five prior years percentage rents actually paid to the Port. This market reset recognizes the cyclical rental amounts the development is able to support while ensuring that the minimum base rent stays above the prior year minimum base rent to protect the Port against inflation.

12. **Percentage Rent:**

During Lease Years 3 to 7: ***(Operation Period Years 1 to 5)***
The amount by which 3.5% of the Annual Gross Revenue from all of the Hotel operations plus 3.5% of the Annual Gross Revenue from all of the Dinner-Theater Operations (Teatro ZinZanni's Operations on the Site) exceeds Minimum Base Rent.

During Lease Years 8 to 12 **(Operation Period Years 6 to 10)**
The amount by which 4.5% of the Annual Gross Revenue from all of the Hotel operations plus 3.5% of the Annual Gross Revenue from all of the Dinner-Theater Operations exceeds Minimum Base Rent.

During Lease Years 13 to 22: **(Operation Period Years 11 through 20)**
The amount by which 5.5% of the Annual Gross Revenue from all of the Hotel operations plus 3.5% of the Annual Gross Revenue from all of the Dinner-Theater Operations exceeds Minimum Base Rent.

During Lease Years 23 to 50: **(Operation Period Years 21 through 48 and Extension Period Years 49 to 64)**
The amount by which 6.5% of the Annual Gross Revenue from all of the Hotel operations plus 3.5% of the Annual Gross Revenue from all of the Dinner-Theater Operations exceeds Minimum Base Rent.

13. Participation Rent:

a. During TZK's Tenancy- the Original Tenant's Tenancy

i. **<u>During Period of No Refinance or Sale</u>**: After TZK has earned 20% IRR on actual equity invested in the project (up to a cap, described below), surplus cash flow shall be shared at (i) 80/20% (TZK/Port) until TZK receives a 25% IRR and then (ii) 50/50% (TZK/Port).

ii. **<u>During Period of Refinance, Assignment, or Sale</u>**: After TZK has earned 20% IRR on actual equity invested in the project (up to a cap, described below), surplus cash flow shall be shared at (i) 80/20% (TZK/Port) until TZK receives a 25% IRR and then (ii) 50/50% (TZK/Port).

b. During Subsequent Tenant's Tenancy

i. **<u>During Period of No Refinance or Sale</u>**: After the Subsequent Tenant has earned 16% IRR on actual equity invested in project, surplus cash flow shall be shared at (i) 80/20% (Subsequent Tenant/Port) until Subsequent Tenant receives an 18% IRR and then (ii) 50/50% (Subsequent Tenant/Port).

ii. **<u>During Period of Refinance, Assignment, or Sale</u>**: After Subsequent Tenant has earned 16% IRR on actual equity invested in project, surplus cash flow shall be shared at (i) 80%/20% (Subsequent Tenant/Port) until Subsequent Tenant receives an 18% IRR and then (ii) 50/50% (Subsequent Tenant/Port).

14. Limits on TZK, Original Tenant, Equity Return and Repayment:

<u>TZK Predevelopment and Construction Equity – Equity Invested Prior to Construction Completion:</u>

TZK is limited to earning 20% IRR on the actual amount of equity invested but not to exceed $60 million.

15. **Limits on TZK, Original Tenant, and Subsequent Tenants, Equity Return and Repayment Once Hotel is Operational**:

a. <u>Tenant Operations Equity - Equity Invested During Operations Period:</u> To provide for funds that may be needed to sustain the hotel operations when there is insufficient operation revenue to cover needed hotel capital or operational costs, Tenant is allowed to invest additional equity for capital improvements and operations (under certain conditions) as follows:

- *Capital Improvements:* Equity invested for defined capital improvements earns 11% IRR; and

- *Operations*: Equity invested for operations to avoid loan default (i.e., debt paydown, debt service shortfall, etc.) or for existing or potential operating shortfalls (i.e., when revenues are insufficient to cover operating expenses due to a demonstrated market-wide downturn) is allowed to earn interest calculated on a simple return basis equal to the lesser of (i) the then interest rate on the then outstanding senior loan on the project, or (ii) 10%. Operations Equity is subject to Port's reasonable consent and approval based on TZK's written notice referencing a market-wide downturn with evidence showing a decrease of 5% or more in San Francisco hotel market Hotel Revenue per Available Rooms ("RevPAR") over the preceding 12-month period. RevPAR is one of the key leading indicators, or metrics, of the hospitality industry's economic health.

d. Cap on Amount of Equity. The equity invested prior to construction completion is limited to $60 million and the equity invested during the operation phase is limited to up to $20 million (inflated at 10-year intervals over the 50-year initial lease term).

16. **Competent Hotel Management Required:** TZK's final selection of a hotel management company or operator is subject to prior review and approval by the Port. The hotel manager must have a minimum number of years of hotel management experience and will be subject to operation standards to maintain.

17. **Sublease**: All subleases are subject to Port's prior consent.

18. **Leasehold Financing**: TZK will have the right to obtain project financing from bona fide institutional lenders secured by its leasehold interest.

19. **No Subordination of Port's Lease Interest:** TZK is not allowed to place any lien on Port's ownership of the Site.

20. **Public Open Space**: TZK is responsible for funding the construction, operation, and maintenance of the public open space during the lease term.

21. **Sea Level Rise**: The Lease will include provisions addressing sea level rise. TZK is required to work with the Port in anticipation of this issue, including implementing flood protection measures determined to be necessary by the Chief Harbor Engineer to protect the building and public health and safety.

22. **City and Other Standard Lease Requirements**: The LDDA and the Lease will include all of the applicable Port and City requirements. They cover such topics as insurance requirements, non-discrimination requirements, hiring policies, indemnity and release, insurance, hazardous materials, casualty, mortgages, maintenance and repair, and all of the other applicable Port and City requirements.

23. **Reversion Interest:** Tenant will own the improvements during Lease term and at the end of the term, at Port's discretion, the Site and its improvements revert back to Port's sole ownership or the Port may require that improvements be removed at TZK's sole expense.

ANALYSIS OF PROPOSED DEVELOPMENT AND BUSINESS TERMS

The following updated analysis is based on the analyses provided in the prior staff reports on this Development, progress made to date on entitlements, and Port-TZK lease negotiations. Economic expectations and market conditions in 2016, when the Term Sheet was endorsed, have changed and continue to change. As such, in late 2018, TZK representatives reported that both the debt and equity market are requiring higher yields because of changes in the capital market; including higher interest rates, tighter underwriting, higher construction costs, and the project profile involving a ground lease, a dinner-theater element, and maintenance of a public park. Therefore, TZK requested that their 18% IRR on the equity invested in the Development be increased to 20% IRR.

Port staff reviewed the request against reports on market trends and also requested HVS, the Port's hospitality consultant on this Development, to research and survey hotel investors about the trend on returns on capital and equity invested in similar hotels. (HVS stands for Hospitality Valuation and Services and it is a division of TS Worldwide.) HVS confirmed that hotel investors are demanding higher yields and that TZK's request is within the reasonable range of investors' yield expectations.

As anticipated in the April 26, 2016 staff report requesting endorsement of the Term Sheet, TZK submitted to Port staff updated proforma reflecting changes to the terms listed in the Term Sheet. Port staff and HVS have reviewed and analyzed the updated proforma, including projected total development costs, revenue and expenses, and estimated returns, and the underlying assumptions supporting the financial projections. Port staff and HVS have also compared the proposed lease terms to terms in comparable leases and other market metrics. The below analysis section of this report assesses the impact of proposed changes to the terms and conditions listed in the Term Sheet.

<u>Summary Conclusion of the Feasibility of the Proposed Development.</u>
This mixed-use Development that includes a boutique hotel (defined as such due to its scale and style); dinner-theater component that will be operated by Teatro ZinZanni; and a waterfront public open space that will be adjacent to The Embarcadero, remains a creative proposal that leverages the Site's attributes. It represents the highest and best use of the Site, based on the City's appraisal of the Site. The underlying fundamentals of San Francisco's hotel marketplace - e.g., strong demand driven by the city's status as one of the world's most favored travel destinations, high-hotel occupancy (currently averaging 80% which exceeds the national average of 66.5%, and constrained supply of hotel rooms – combined with the recent completion of the Moscone Center Expansion drawing more conventions to the City, the Chase Center

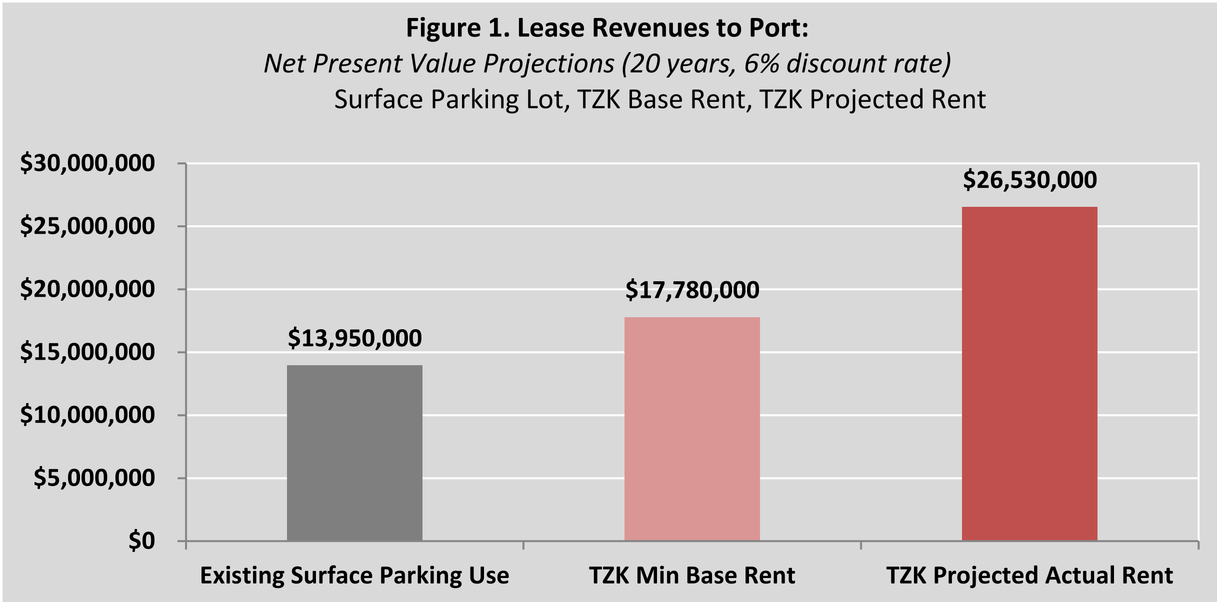
Arena drawing NBA fans to the City, and Site's waterfront location, all clearly provide support for the proposal.

The Development continues to be deemed financially feasible with the recent revisions made to the development's floor layout concept and the related development assumptions. While the estimated total development cost has increased from $124 million to $142 million, an increase of about 15%; this increase has been offset with increase in projected occupancy, while the project hotel room rates have been decreased to reflect the reduction of the hotel's average room size. This reduction has been offset with the increased in the hotel's total room count. The continuing feasibility of the Development remains based on a number of key assumptions. These assumptions include that the current estimated construction costs will remain within or near to the projected total development cost plus estimated contingency; that there will not be significant building permit delays; that the real estate capital market will remain stable with no spikes in interest rates or dramatic change in commercial loan underwriting, and that the economy in general will remain stable.

The proposed lease payment terms are set to ensure that the minimum base rent to the Port exceeds the current revenues generated by the surface parking lot. **Figures 1** and **2** illustrate a 20-year projection of lease revenues to the Port from:

- **Existing use.** Surface parking operations (based on the last four years of operations and five-year revenue projections from Port staff).
- **Proposed hotel development, base rent.** TZK minimum base rent as escalated to date (assuming no market resets, as described in (11), above).
- **Proposed hotel development, projected rent.** TZK projected rent to the Port (based on hotel revenue projections).

As shown, the existing use is projected to generate $13.95 million over next 20 years (in net present terms) compared to the guaranteed minimum base rent expected to be included in the proposed lease to generate $17.7 million and the projected rent to the Port of $26.5 million from percentage and participation rents expected to be included in the proposed lease. Note that a longer projection (e.g., through years 50 or 66) would show an even greater divide between the financial outcomes to the Port from the continued use of the land as a surface parking lot compared to the proposed hotel development.



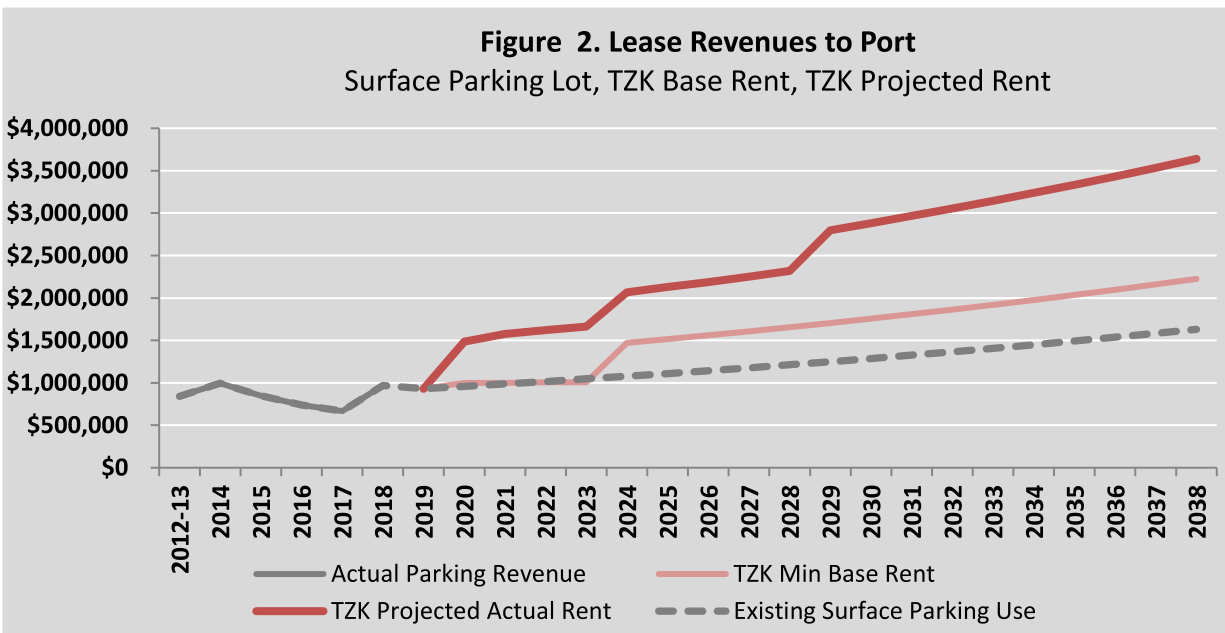


Table 3 presents projected gross revenues for the hotel operations (from lodging, food and beverages and miscellaneous operations), projected gross revenues for Teatro's dinner-theater operations (from ticket sales, food and beverages and miscellaneous operations), minimum base rents to the Port with annual escalations, percentage rent, and the expected high and low annual net rent to the Port under the lease based on the negotiated terms. Rows 16 and 30 in **Table 3** presents net projected annual rent to the Port starting from construction period at $1 million per year and gradually increasing to $2.31 million in Operational Year 10 and $3.64 million in Operational Year 20.

Focusing only on negotiated minimum base rents, projected (minimum base) rent starts from $1 million (Rows 4) and increases through annual escalations and market resets to approximately $2.431 million per year in the 20th year of the development operation phase (Row 20). Percentage rent is projected to generate $1.577 million per year from Operational Year 3 (Row 13) and rises through a series of preset percentage rate increase, from 3.5% against all gross revenues to 4.5% and 5.5% against hotel gross revenue plus 3.5% against the dinner-theater gross revenue to approximately $3.64 million per year in the 20th year of the development operation (Row 30). Percentage rent increases once more during the lease term, to 6.5% against hotel gross revenue plus the 3.5% against the diner-theater gross revenue, in the 21st year of the development operation phase.

Projected gross revenue for the hotel and dinner-theater is forecasted at $38.968 million for the first year of operations, increasing to $54.827 million by the 10th year of operations, and continued increases to approximately $73.462 million by the 20th year of operations. These projections have been re-verified and reconfirmed as feasible by HVS and Port staff due diligence. Assuming the current capital market assumptions continue to hold, the current forecasted revenues support the estimated $60 million of equity and $82 million of debt proposed to fund the $142 million of estimated total development cost.

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Table 3 - Projected Revenues based on Negotiations for the Lease Years 1 to 22
Projected Lease revenues for the Port ($000s)

		Entitlement Period					Construction Period		Operation Period									
									Stabilization Period		Full Operation Period							
									Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10
Base Year	Factor	**2015**	**2016**	**2017**	**2018**	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**	**2030**	**2031**
1 Base Rent		$1,100	$1,133	$1,167	$1,202	$1,238	$1,275	$1,313	$1,353	$1,393	$1,471	$1,515	$1,561	$1,607	$1,656	$1,705	$1,756	$1,809
2 Base Rent Annual Escalation	3.00%																	
3 Applicable Minimum Base Rent		$1,100	$1,133	$1,167	$1,202	$1,238	$1,275	$1,313	$1,353	$1,393	$1,471	$1,515	$1,561	$1,607	$1,656	$1,705	$1,756	$1,809
4 Negotiated Minimum Base Rent							**$1,000**	**$1,000**	**$1,007**	**$1,007**	**$1,471**	**$1,515**	**$1,561**	**$1,607**	**$1,656**	**$1,705**	**$1,756**	**$1,809**
5 Compare: Baseline Row 2 to TZK Negotaited Minimum Base Row 4							78%	76%	74%	72%	100%	100%	100%	100%	100%	100%	100%	100%
6 Gross Hotel Revenue	3.00%								$27,506	$30,673	$32,882	$33,794	$34,525	$35,542	$36,689	$37,667	$38,778	$39,922
7 Gross Theater Revenue	3.00%								$11,462	$11,820	$12,185	$12,568	$12,941	$13,311	$13,692	$14,085	$14,489	$14,905
8 Combined Revenues									$38,968	$42,494	$45,068	$46,361	$47,466	$48,852	$50,381	$51,752	$53,267	$54,827
9 Negotiated Percentage Rent																		
10 From Hotel Operations Years 1 though 5	3.50%								$963	$1,074	$1,151	$1,183	$1,208					
11 From Hotel Operations Years 6 though 10	4.50%													$1,599	$1,651	$1,695	$1,745	$1,796
12 From Theater Operations	3.50%								$401	$414	$426	$440	$453	$466	$479	$493	$507	$522
13 Total Percentage Rent									**$1,364**	**$1,487**	**$1,577**	**$1,623**	**$1,661**	**$2,065**	**$2,130**	**$2,188**	**$2,252**	**$2,318**
14 Minimum Base Rent Adjustment at end of Year 10																		
15 65% of the average of the 5 prior years	65% (This no longer applies)																	$1,424
16 Expected Lease Payment to Port							**$1,000**	**$1,000**	**$1,364**	**$1,487**	**$1,577**	**$1,623**	**$1,661**	**$2,065**	**$2,130**	**$2,188**	**$2,252**	**$2,318**

		Operation Period									
		Full Operation Period									
		Years									
		11	**12**	**13**	**14**	**15**	**16**	**17**	**18**	**19**	**20**
		2032	**2033**	**2034**	**2035**	**2036**	**2037**	**2038**	**2039**	**2040**	**2041**
17 Base Rent		$1,863	$1,919	$1,977	$2,036	$2,097	$2,160	$2,225	$2,292	$2,361	$2,431
18 Base Rent Annual Escalation	3.00%										
19 Applicable Minimum Base Rent		$1,863	$1,919	$1,977	$2,036	$2,097	$2,160	$2,225	$2,292	$2,361	$2,431
20 Negotiated Minimum Base Rent		**$1,863**	**$1,919**	**$1,977**	**$2,036**	**$2,097**	**$2,160**	**$2,225**	**$2,292**	**$2,361**	**$2,431**
21 Compare: Baseline Row 2 to TZK Negotaited Minimum Base Row 4		100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
22 Gross Hotel Revenue		$41,100	$42,314	$43,564	$44,852	$46,179	$47,545	$48,952	$50,401	$51,894	$53,431
23 Gross Theater Revenue		$15,352	$15,813	$16,287	$16,776	$17,279	$17,797	$18,331	$18,881	$19,448	$20,031
24 Combined Revenues		$56,453	$58,127	$59,852	$61,628	$63,458	$65,342	$67,283	$69,282	$71,342	$73,462
24 Negotiated Percentage Rent											
25 From Hotel Operations Years 11 though 20	5.50%	$2,261	$2,327	$2,396	$2,467	$2,540	$2,615	$2,692	$2,772	$2,854	$2,939
26 From Theater Operations	3.50%	$537	$553	$570	$587	$605	$623	$642	$661	$681	$701
27 Total Percentage Rent		**$2,798**	**$2,881**	**$2,966**	**$3,054**	**$3,145**	**$3,238**	**$3,334**	**$3,433**	**$3,535**	**$3,640**
28 Minimum Base Rent Adjustment at end of Year 20											
29 60% of the average of the 5 prior years	65% (This no longer applies)										$2,233
30 Expected Lease Payment to Port		**$2,798**	**$2,881**	**$2,966**	**$3,054**	**$3,145**	**$3,238**	**$3,334**	**$3,433**	**$3,535**	**$3,640**

ANALYSIS OF THE PROPOSED TERMS AND CONDITIONS

Development Benefits

Based on real estate consultant reports and market comparables, Port staff analysis of the lease terms being proposed resulted in the following conclusions:

1. Adequate Rent Structure and Financeable Project: The rent structure is on par or higher than comparable recent leases in the San Francisco Bay Area, particularly for small or boutique hotels. Port staff ordered a hotel ground rent survey and reviewed the pertinent comparables and their related rental rates. The comparables indicated that the base rent and percentage rent to include in the proposed lease are competitive and at market rate given the economic profile for the Site and the Development.

Most hotel ground leases do not provide for the landlord to participate in the development upside other than through percentage rent against gross revenue. The proposed deal provides for the Port to participate in all development upsides, including profits from refinancing, assignments and sales. In return, the Port is allowing TZK to earn a hurdle rate on equity limited to 20% internal rate of return, or IRR, prior to additional revenue sharing with the Port. Once the developer earns a 20% IRR, surplus cash flow is required to be shared with the Port at 80/20% to TZK/Port until TZK attains a 25% IRR at which time the share of further surplus cash flow is 50/50% to TZK/Port.

As indicated earlier in this Memorandum, the change to 20% IRR with 80%/20% (TZK/Port) split of excess cash flow is supported by Port staff and HVS analyses, updated market research, and feasibility modeling, and the goal of this change is to make the proposed development financeable while limiting Port downside.

HVS has conducted further market research and confirmed that 80%/20% split between the TZK and Port, over a 20% IRR is within a supportable position based on changes in the capital market conditions since Term Sheet was endorsed about 36 months ago. HVS's analysis indicates 80%/20% split over 20% IRR would achieve the goal of making the Development financeable and is consistent with current market expectations. Based on HVS's input, Port staff concluded that accepting a term similar to what TZK has proposed, in exchange for additional protections for the Port's financial share of the participation. The protection measures were discussed earlier in this Memorandum and include: limiting the amount of equity which would receive the 20% IRR ("equity cap"); segmenting equity invested into tiers ("tiering"), and requiring Port's consent to additional equity investment during the operation phase.

2. Proposed Deal Structure Improves the Development Competitiveness: The proposed terms will allow TZK to induce the necessary capital investment for the development. While the minimum base rent and percentage rent increase as the term left on the lease decreases, the lease terms/conditions provided in the proposed deal structure combined with the potential high upside in San Francisco's hotel market provides sufficient incentives to induce fresh investment capital to maintain the competitiveness of this facility.

3. Maximum Port Leverage: There is no Port funding for any part of the Development and all costs incurred by the Port in the transaction connected to the development are to be paid by the TZK. These costs include Port staff costs, Port consultant costs, and Port attorney costs.

4. Economic Benefits: Expected benefits of the proposed development include, among other things, an architecturally-fitting, urban edge to the eastern boundary of the Northeast Waterfront Historic District and a welcoming and an activating gateway to North Beach and Chinatown. Other significant benefits include property, hotel, sales, and gross receipts taxes and other direct and indirect revenues for the City. The Development is anticipated to generate approximately 550 construction jobs, and over 350 permanent and part-time jobs.

5. Tax Increment Financing Opportunity: Another benefit of the proposed development is the opportunity, under the Port's Infrastructure Financing District policy, to generate new funds for the Port Capital Plan or Port's Seawall Rehabilitation project. Both programs are in need of additional funding mechanisms.

   Port staff, therefore, are taking steps to support activation a new subarea boundary around the Site, within the Port's Infrastructure Financing District consistent with IFD law (Gov't Code §§ 53395-53397.11) and the City's *Guidelines for the Establishment and Use of an Infrastructure Financing District with Project Areas on Land Under the Jurisdiction of the San Francisco Port Commission*,[7]. Staff will request that the Port Commission direct Port staff to seek approval of the Board of Supervisors to add the Site to the existing Portwide IFD to capture future growth in property taxes that will occur as a result of this theater-hotel development.

   The new IFD subarea will capture the City's share of tax increment (about 65 percent) from the Site for 45 years. Tax increment from the new IFD subarea could be used to fund historic rehabilitation and sea level rise protection improvements, as alternatives to the Seawall Rehabilitation project.

6. Retention of Cultural Venue: The proposed Development will help sustain culture and arts in the City. Specifically, it will reinforce the City's commitment pursuant to City Administrative Code Chapter 90A, encouraging support for

[7] For a copy of Board of Supervisors Resolution 123-13 related to the policy, see: https://sfgov.legistar.com/LegislationDetail.aspx?ID=1323177&GUID=19D641A0-A64B-4F34-B428-D7C7FCD037A4&Options=ID|Text|&Search=130264

accommodating cultural venues on available City properties to prevent displacement of such venues.

7. The final terms negotiated include provisions addressing or limiting potential exposure of Port to risks including development, cost, and market risks, among others (described further below).

Development Risks

The Port owns the Site unencumbered and the Site is currently generating about $969,000 per year as of June 2018 in net revenue to the Port. The current parking operation is an interim use not representing the Site's highest and best use. The proposed Development does pose some risks to the Port most of which can be mitigated through the LDDA and the Lease requirements, including construction and minimum rent provisions. The Development represents the Site's highest and best use with greater economic benefit for the Port and the City (relative to its current use) and includes a major investment of private capital into Port property which will revert to the Port at the end of the lease.

1. Hotel Development Risk

   Considered high-risk/high-reward investments, hotels usually pose challenges in exposure to seasonality (swings in demands) and in asset valuation. As with all hotel developments, the proposed hotel will combine real estate with an operating business, and it will have high operating leverage and some economic sensitivity, in seasonality from hotel room demand. It also will be management, marketing, energy and capital intensive. Despite all these challenges, this hotel is expected to generate favorable long-term yields as a quality real estate investment given its many favorable attributes. It is in San Francisco at a premium location on the waterfront and it is of a scale that will sustain desirable occupancy over the long term. To mitigate the operating risk, the Port will insist on the hotel manager meeting certain prerequisites and that the manager-selection be subject to Port's prior consent. Port's exposure to this risk is limited to not receiving percentage rent at the levels currently anticipated, which can be mitigated by including performance standards in the Lease and in the hotel management agreement.

2. Entitlement Risk

   The developer has received all entitlements except for Building Permit which it on track to obtain once it has full site-control through approval of the proposed Transaction Documents. Port's exposure to this risk is considered minimal both under its proprietary role as a landowner and as a regulator.

3. Financing Risk

   Given the current low-interest rate environment, and the desirable quality of this hotel located in a high-tourist and business travelers area that has a limited supply of hotels, the availability, and cost of, funds are expected to be supportive of the proposed Development. The Port's exposure to this risk is minimal since the Port is not providing any capital funding for the Project and the Site will not be transferred to the Developer until all required financing is in place and escrow is closed.

4. Cost Risk

The Project is subject to the expected increases of construction costs until TZK has entered into a binding construction contract with a fixed price, if the remaining project approvals take longer than the Developer had planned. Measures to mitigate this risk include cost projections that provide ample construction contingency, using guaranteed maximum pricing for the construction contract, providing for performance and payment bonds, and using competent project managers. Port's exposure to this risk is considered minimal since the Port is not providing any capital funding for the Project. If there are cost overruns and the Developer has to invest more money into the project, it may take longer for the Port to share in the Development's surplus cash flow through percentage and participation rents, although the cap on initial equity will lessen this impact.

5. Market Risk

Market, competition, and business cycle risks for the proposed development are considered minimal given the supply and demand conditions of the hotel market. Competition with larger hotels, online travel agencies, and Airbnb[8], however, has been given adequate attention. This competition can be addressed given the advantages the Site bestows on the Development, amongst which is its proximity to many San Francisco attractions. Through competent hotel management with proactive stance on marketing and competition, these risks can be mitigated. Another risk that has been addressed is a systemic or externality risk from market-wide downturn, like economic recession. This risk is being addressed through a provision allowing TZK to invest additional or operations equity discussed earlier in this Memorandum to fund operation shortfalls or pay down debt to avoid potential loan default. Port's exposure to this category of risks is considered minimal and it is limited to the percentage rent and further mitigated through guaranteed minimum base rent.

6. Counterparty Risk

This risk usually arises from poor project oversight brought on by lack of requisite development expertise and financial capacity. TZK members have the qualifications and financial capacity to perform as a developer and project managers. In June 2015, Kenwood Investments provided the Port a description of its qualifications and financial capacity. BAE Urban Economics, a Port-hired, third-party real estate consultant ("BAE"), and Port staff reviewed the qualifications and financial capacity information. BAE issued a report confirming that Kenwood Investments is qualified to develop the Project. Port staff filed the report with the Clerk of the Board of Supervisors on August 18, 2015.

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[8] **Airbnb** is an online service that facilitates the listing, finding, and renting of lodging. It has listings in San Francisco and other cities.

In 2018, TZK provided Port staff information on Presidio's financial wherewithal and experience, particularly with hotel development capitalization, management, and operation. Presidio is reported to have owned and operated, and continues to own and operate, independent boutique properties, full-service conference center hotels, full-service resort hotels as well as select- and limited-service hospitality properties at different locations across the United States. Presidio has demonstrated that it has both the experience and financial standing to assist TZK in achieving the ultimate goal of a new home for Teatro ZinZanni in San Francisco and a successful hotel on the Site. With Presidio on board, TZK improved the hotel's interior layout to increase efficiency and save costs, identified possible capital sources to invest in the development, and bringing on board franchisor that is expected to be a good fit for this hotel with its unique attributes.

Port's exposure to this risk is considered minimal and it is mitigated by requiring the developer to reimburse all Port costs related to this transaction and further mitigated by not closing escrow until all preconditions to escrow closing are met, including lenders' requirements for proof of the required equity in the amount needed to close escrow on construction loan.

7. Operating Risk

This risk usually arises from inadequate budgeting, planning and project management. This risk is being mitigated by requiring competent project manager and hotel operator who can maintain high occupancy with high revenue per room and meet pro-forma expectations. The Port's percentage rent income is dependent on the hotel management. Port's exposure to this risk, however, is considered minimal and mitigated through guaranteed minimum base rent and including performance standards in the Lease and in the proposed hotel management agreement.

This is risk is being further mitigated by allowing the TZK to invest equity, "Operations Equity," during the operation phase to fund operation shortfalls or head-off a loan default brought on by a market-wide economic downturn. This Operation Equity is subject to the limitations discussed earlier in this Memorandum under *Item #15* under the **Summary of Proposed Lease Terms**. Port staff has negotiated an appropriate metric to measure hotel market-wide downturn or area-wide downturn that the Port will ascertain before letting TZK invest these Operations Equity. The Port will review the decrease in *revenue per available rooms or "RevPAR*" over a 12-month period with a minimum 5% cumulative decrease for the geographical area encompassing the competitive set of hotels for this proposed hotel. The geographically area currently is the entire San Francisco hotel market. TZK will be required to provide a notice to the Port about the downturn supported with evidence of the downturn. HVS has recommended STR's report tracking changes in RevPAR as an acceptable source for this evidence.

FURTHER PROJECT REVIEW

Port staff, with assistance from HVS, will continue to review and analyze updated information about the hotel market, comments from the Port Commission, and updates from the developer. The result of this ongoing review and analysis will be addressed in the next Port staff report to the Port Commission in seeking its consideration and approval of the final deal terms to include in the LDDA and Lease.

Community Outreach

Representatives of TZK and Teatro ZinZanni remain committed to thorough public involvement in the review of the proposed development. They have continued to conduct engaging outreach to stakeholders, including meeting with the Barbary Coast Neighborhood Association, Golden Gateway Tenants Association and Gateway Commons Board of Directors. With assistance from Port staff, they have presented updates on the proposed development to the Northeast Waterfront Advisory Group ("NEWAG"). Members of NEWAG continue to express support for the proposals. Both Port staff and the TZK and Teatro representatives will continue to apprise NEWAG of key project developments.

Approval Process

TZK has completed most of the key tasks it is required to complete under the ENA as reported earlier in this staff report. TZK has completed CEQA evaluation that resulted in a Final Mitigated Negative Declaration that includes certain mitigation measure to lessen the impact of the construction and operation of the development on the environment. It has procured all required land use entitlements, Conditional Use Authorization for the Hotel and Planning Commission support for the proposed street vacation and lots merger for a unified development parcel. It has also completed negotiation of final terms and conditions of the LDDA and the Lease, and it's now planning to seek Port Commission approval of the LDDA and Lease during the next Port Commission public meeting set for September 10, 2019.

Timeline/Next Steps

Complete lease negotiations	August-Sept. 2019
Port Commission approval of the LDDA and Lease	September 2019
Board of Supervisors' approval of the Lease	October 2019

Prepared by: Ricky Tijani
Development Project Manager

Through: Rebecca Benassini, Assistant Deputy Director
Waterfront Development

For: Michael Martin, Deputy Director
Real Estate & Development

Exhibits:	“A”	Site Map
	“B”	Proposed Project Schematic Drawings
	“C”	A Summary of the Key Business Terms from the Term Sheet
	“D”	Benefits of the Development to the Public Trust

Exhibit "A"
Site Map

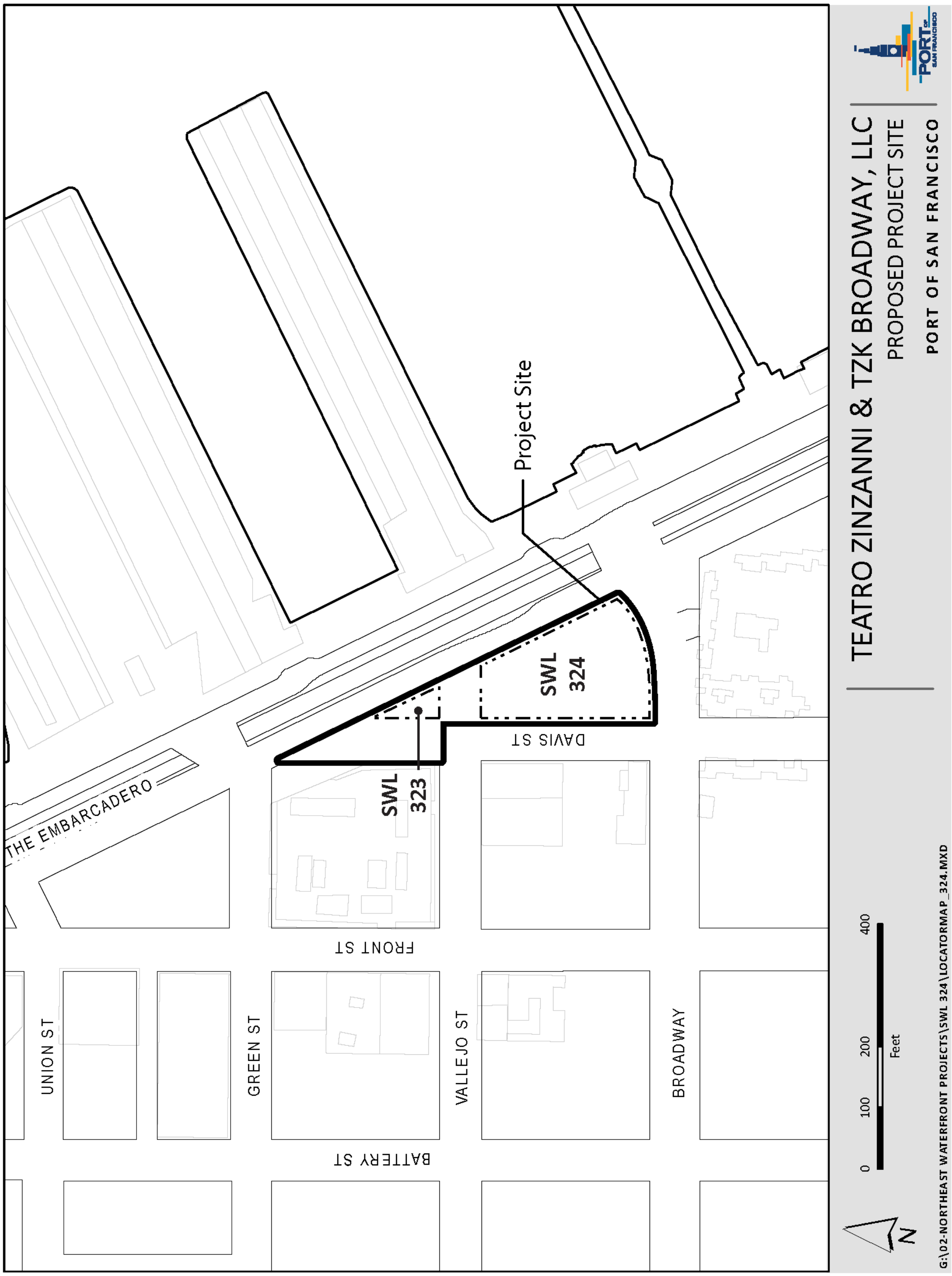
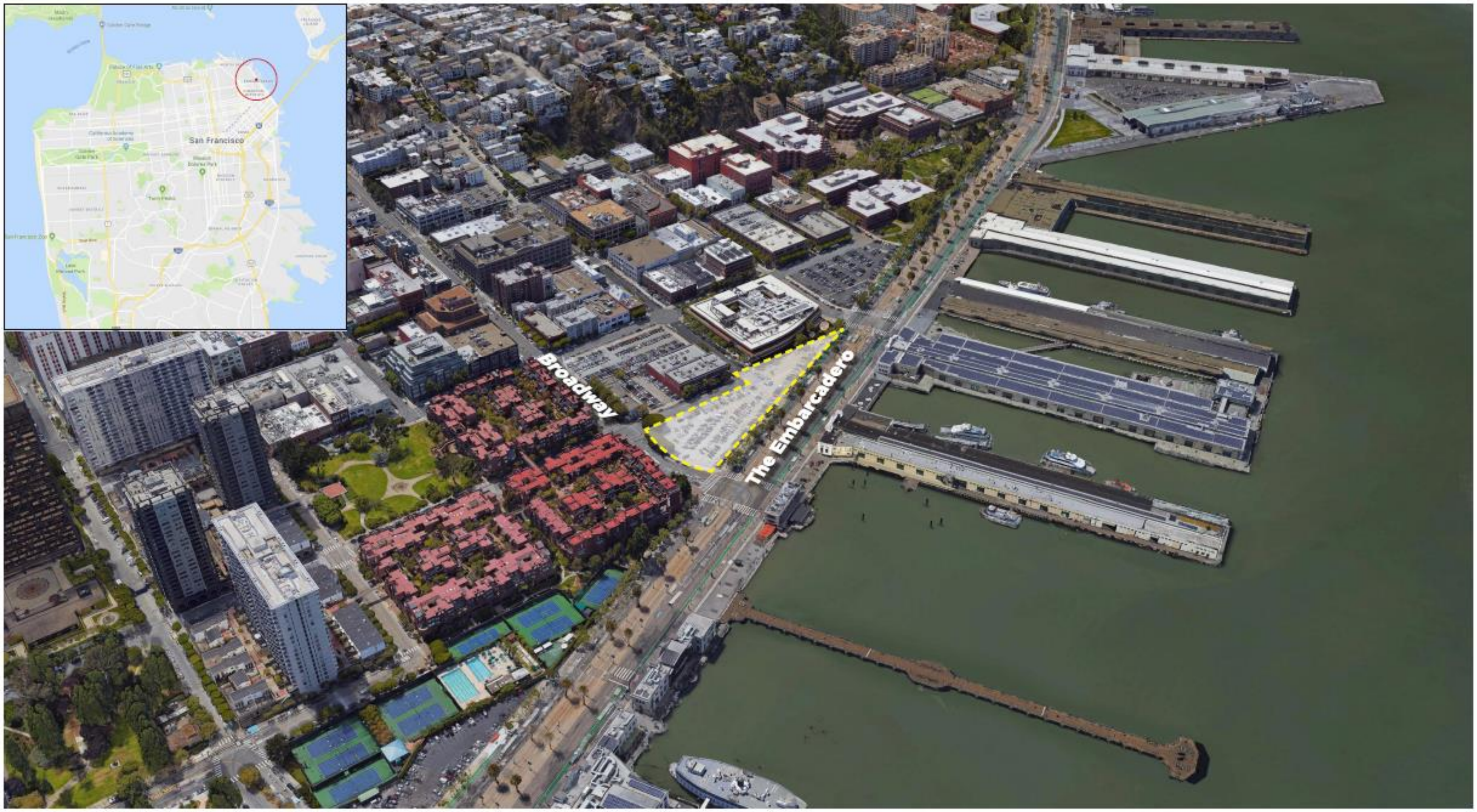


Exhibit “B”
Proposed Project Schematic Drawings



Project Location at Embarcadero & Broadway

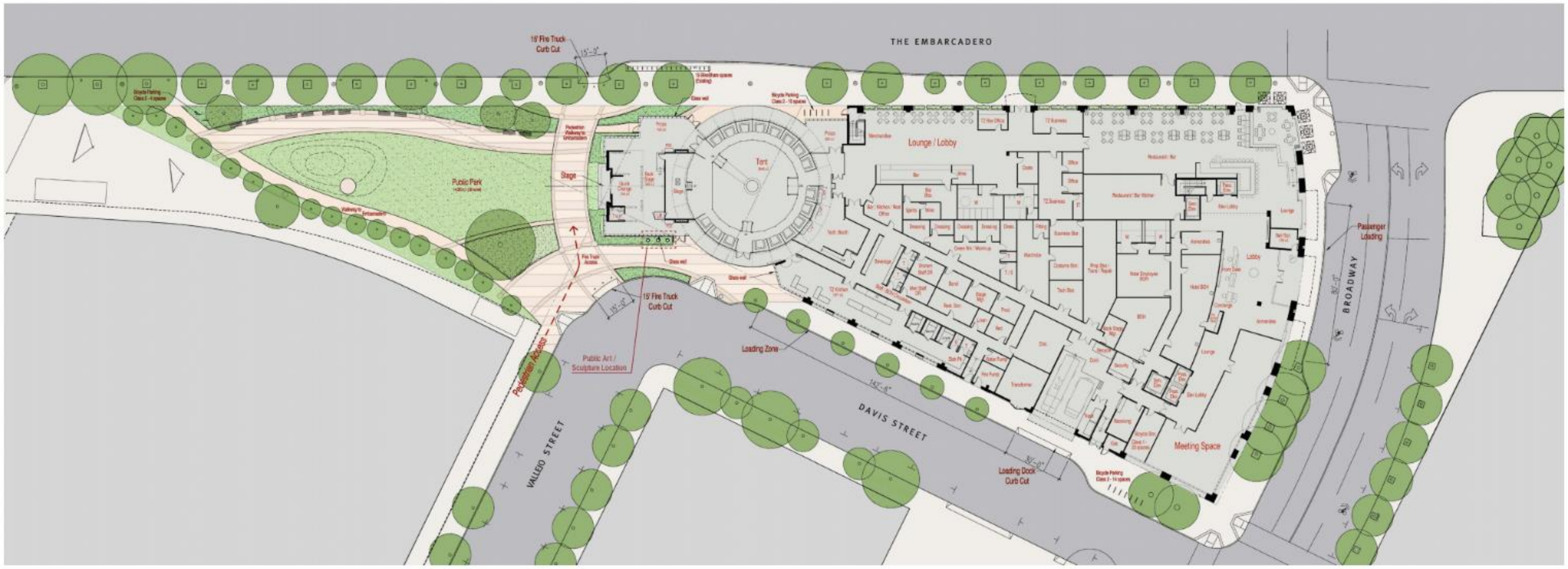
May 2, 2019 | 1

Teatro ZinZanni presidio companies
KENWOOD INVESTMENTS

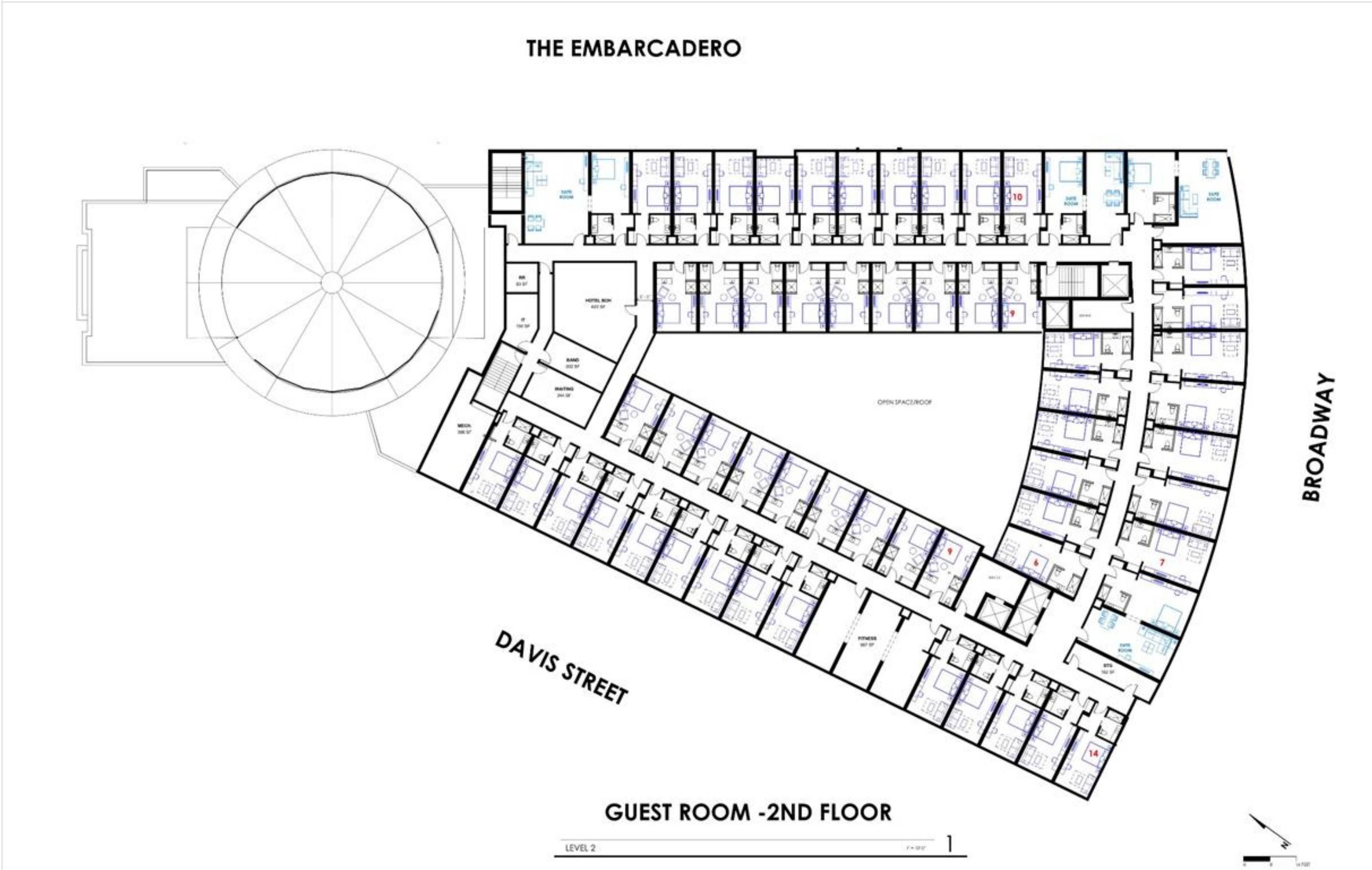
The Theater & Hotel @ Broadway | Seawall Lots 323/324, San Francisco, CA
A Teatro ZinZanni & Kenwood Investments Project

Hornberger + Worstell Architects

Hornberger + Worstell



Site Plan / Park and Public Realm


THE EMBARCADERO
BROADWAY
DAVIS STREET
GUEST ROOM -2ND FLOOR
LEVEL 2
1

Broadway

The Embarcadero

Building Elevations

Teatro ZinZanni
KENWOOD INVESTMENTS

ZinZanni / Kenwood - The Theater & Hotel @ Broadway | San Francisco, California
A Teatro ZinZanni & Kenwood Investments Project

presidio companies HR

Park

Davis Street

Building Elevations

Teatro ZinZanni
KENWOOD INVESTMENTS

ZinZanni / Kenwood - The Theater & Hotel @ Broadway | San Francisco, California

A Teatro ZinZanni & Kenwood Investments Project

presidio companies HR

Public Park As Neighborhood Amenity

Public Park and ZinZanni Pavilion

May 2, 2019 | 10

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The Theater & Hotel @ Broadway | Seawall Lots 323/324, San Francisco, CA
A Teatro ZinZanni & Kenwood Investments Project

Hornberger + Worstell Architects

Hornberger + Worstell

Visual Analysis | **Park View from Davis Street**

TEATRO ZINZANNI
KENWOOD INVESTMENTS

ZinZanni / Kenwood - The Theater & Hotel @ Broadway | San Francisco, California
A Teatro ZinZanni & Kenwood Investments Project

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View South Along The Embarcadero

TEATRO ZINZANNI
KENWOOD INVESTMENTS

ZinZanni / Kenwood - The Theater & Hotel @ Broadway | San Francisco, California
A Teatro ZinZanni & Kenwood Investments Project

presidio companies HR

Exhibit "C"
Summary of the Key-business terms from the Term Sheet
(Annotated to indicate which terms have changed and what the changes are)

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
1.	Site	SWLs 323/324 + two street stubs	No Change
2.	Lease Effective Date	At Close of Escrow under the LDDA	No Change
3.	Lease Term	• Initial Term: 50 years • One 16-year extension option subject to conditions.	No Change
4.	Development Program	• 192 Hotel rooms, approximately • 10 Extended Stay rooms for artists • Ground level retail/commercial space • Teatro's dinner-theater program • Privately funded 7,500 sf open space/park.	Changes: • Eliminated extended stay rooms for artists • Privately funded open space/park size confirmed at 14,000 sf
5.	Total Development Cost and Funding	• $134,000,000 • $74,000,000 – Debt • $60,000,000 – Initial Equity	Changes: • $140,530,000 • $83,000,000 – Debt • $30,000,000 - EB-5 Equity • $2,500,000 – Marriot & Interstate Key Money • $25,026,034 – Third Party/Sponsor Equity
6.	LDDA, Fee and Extension	• Term: 24 months • $37,500/year in LDDA Fee • 12 months to COE from Effective Date • First 6-month extension to close Escrow is subject to $50,000 fee • Second 6-month extension is subject to $50,000 fee • Transaction Cost Recovery provided • Liquidated Damage for delay in Construction Completion: TZK to pay Port $1,150 for each day	Essentially No Change • Four 3-month extensions to close Escrow is subject to $25,000 fee per each extension (still 12 months at cost of $100,000) • Liquidated damage amount remains the same. Four 3-month extension periods (still a total of 12 months of extension beyond the 24-month construction period). Each 3-month

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
		after the total of 36 months to complete construction (the initial 24-month period plus the two 6-month extension periods).	extension requires a $25,000 fee. $1,115 starts at the end of the 36-month period.
7.	LDDA Termination Fee	A $50,000 fee for terminating the LDDA plus assignment of work-products. A third party actual use of the work-product is subject to negotiations at that time in the future. Termination is stayed during a Force Majeure Event.	No Change
	Appraised FMV Appraised FM Rent	Appraisal completed on April 15, 2015 Appraised FMV: $16.65 million Appraised Fair Market Rent: $1.1 million per year Appraisal Recommended Escalation: CPI every 5-year	Negotiated Minimum Based Rent set in 2016 escalated to account for the current approximately 2-year lapse.
8.	Construction Period Rent	• **$890,000 per year** based on the recent highest revenues from parking operation. • Anticipated Construction Period as of April 26, 2016: 2017 to 2018	• **$890,000 per year** based on the recent highest revenues from parking operation. • Anticipated Construction Period as of April 2019: **2020 to 2021**
9.	Lease Full Operation Period Rent	**First Period: Years 1 through 5**: Stabilization Period, Year 1 (2019) and 2 (2020) of operations: Minimum Base Rent: The Greater of: **(a) $915,000 per year** Or (b) 3.15% (90% of 3.50%) of Hotel Gross Revenues if Occupancy reached 80%. Full Operation Period, Years 3-5 of operations: Greater of: (a) **$1,366,000** escalated between 2.5% to 3.5% annually based on CPI Or	**First Period: Years 1 through 5**: Change Minimum Base Rent: The Greater of: **(c) $1,007,000 per year** Full Operation Period, Years 3 (2024) Year 4 (2025) and Year 5 (2026) of operations: Change (a) **$1,471,000** escalated between 2.5% to 3.5% annually based on CPI

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
		(b) 3.5% of Hotel Gross Revenues plus 3.5% of Theater-Dinner operations **Second Period: Years 6 through 10**: The Greater of: (c) **$1,471,000** escalated ~~3%~~ 2.5% to 3.5% annually based on CPI Or for the next five years: (d) 4.5% of Hotel Gross Revenues plus 3.5% of Theater-Dinner operations	**Second Period: Years 6 through 10**: Change (a) **$1,623,000** escalated ~~3%~~ 2.5% to 3.5% annually based on CPI
		Third Period: Years 11 through 20: (e) Minimum base rent **Reset** at the greater of: 65% of the average of the prior 5 year percentage rent escalated ~~3%~~ 2.5% to 3.5% annually based on CPI or Prior year's minimum base rent plus 2.5-3.5% based on CPI Or (f) 5.5% of Hotel Gross Revenues plus 3.5% of Theater-Dinner operations	**Third Period: Years 11 through 20**: No Change
		Fourth Period: Years 21 through 50: The Greater of: (g) Minimum base rent escalated by between 2.5% and 3.5% based on CPI annually and Reset every 10 years to the greater of 65% of the average of the prior 5 year percentage rent or Prior year's minimum base rent plus 2.5-3.5% based on CPI Or : (h) 6.5% of Hotel Gross Revenues plus 3.5% of Theater-Dinner operations Minimum rent to adjust to fair market rent every 10 years.	**Fourth Period: Years 21 through 50**: No Change

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
		Minimum rent to escalate annually between ~~3%~~ 2.5% to 3.5% annually based on CPI.	
10.	Rent Credit	**No Rent Credits**	No Change
11.	Public Park	Public Park total development, operation and maintenance costs are TZK's sole responsibility during the Lease term.	No Change
TZK, the Original Tenant, Actual Equity invested Prior to Construction Completion			
12.	TZK Equity Repayment and Return of Equity	TZK is limited to earn 18% IRR and after earning the 18% IRR, surplus cash flow shall be shared at (i) 70/30 (TZK/Port) until TZK receives a 25% IRR and then (ii) 60/40 (TZK/Port).	TZK is limited to earn ~~18%~~ 20% IRR and after earning the ~~18%~~ 20% IRR, surplus cash flow shall be shared at (i) ~~70/30%~~ 80%/20% (TZK/Port) until TZK receives a 25% IRR and then (ii) ~~60/40%~~ 50/50% (TZK/Port).
13.	Participation Rent: (Port's Share of Project Revenues)	**During Period of No Refinance or Sale**: After TZK has earned 18% IRR, TZK and surplus cash flow shall be shared at (i) 70/30 (TZK/Port) until TZK receives a 25% IRR and then (ii) 60/40 (TZK/Port).	**During Period of No Refinance or Sale**: After TZK has earned ~~18%~~ 20% IRR, surplus cash flow shall be shared at (i) ~~70/30%~~ 80%/20% (TZK/Port) until TZK receives a 25% IRR and then (ii) ~~60/40%~~ 50/50% (TZK/Port).
14.	Participation Rent: (Port's Share of Project Revenues)	**During Period of Refinance, Assignment, or Sale**: After TZK has earned 18% IRR, surplus cash flow shall be shared at (i) 70/30 (TZK/Port) until TZK receives a 25% IRR and then (ii) 60/40 (TZK/Port).	**During Period of Refinance, Assignment, or Sale**: After TZK has earned ~~18%~~ 20% IRR, surplus cash flow shall be shared at (i) ~~70/30%~~ 80%/20% (TZK/Port) until TZK receives a 25% IRR and then (ii) ~~60/40%~~ 50/50% (TZK/Port).
Subsequent Tenant Actual Equity invested in Purchase of the Leasehold Interest			

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
15.	Subsequent Tenant Equity Repayment and Return of Equity	These returns were not explicitly addressed in the Term Sheet	The Subsequent Tenant is limited to earn 16% IRR with a 20% share to Port afterwards and after earning the 18% IRR, surplus cash flow shall be shared at (i) 50/50% (ST/Port) thereafter.
16.	Participation Rent: (Port's Share of Project Revenues)	These returns were not explicitly addressed in the Term Sheet	The Subsequent Tenant is limited to earn 16% IRR with a 20% share to Port afterwards and after earning the 18% IRR, surplus cash flow shall be shared at (i) 50/50% (ST/Port) thereafter.
17.	Participation Rent: (Port's Share of Project Revenues)	These returns were not explicitly addressed in the Term Sheet	The Subsequent Tenant is limited to earn 16% IRR with a 20% share to Port afterwards and after earning the 18% IRR, surplus cash flow shall be shared at (i) 50/50% (ST/Port) thereafter.
	TZK, the Original Tenant, Actual Equity invested After Construction completion		
18.	TZK Equity Repayment and Return of Equity invested during Operation Period	These returns were not explicitly addressed in the Term Sheet	a. All Capital Improvements Equity invested during operations phase gets an 11% IRR, for both Original Tenant and Subsequent Tenant. b. "Operations Equity" will be recognized, subject to the following: i. **Reasonable consent.** Subject to Port approval, in its reasonable discretion; "Reasonable" standard will include need for equity infusion is market-wide downturn ii. **Simple and subject to capped interest rate.** Operations Equity will earn interest calculated on a simple return basis equal to the lesser of (i) the then interest rate on the then outstanding senior loan on the project, or (ii) 10%. ii. **Defined events**. "Operations Equity" will only include equity contributed during the operations phase to cure loan defaults

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
			or avoid potential loan defaults (i.e., debt pay downs, debt service shortfalls, etc.) or for existing or potential operating shortfalls (i.e., when revenues are insufficient to cover operating expenses), in either event, arising out of market-wide downturns. iv. **Cap on amount**. Up to $20M in additional equity may be invested in the project, on a cumulative basis over the life of the lease. $20M cap will be subject to the following schedule showing increases at 10-year intervals over the 50-year initial lease term.
19.	Reimbursement of Port Transaction Costs	During LDDA term, TZK to pay transaction cost similar to the ENA transaction cost provisions subject to no cap per year and Quarterly advance deposit is required.	Port Transaction Cost recovery during the normal LDDA Period is capped at $300,000. If the LDDA period is extended because of litigation, the cap will be lifted to cover the more than expected Port cost.
20.	Competent Hotel Management Required	TZK's final selection of a hotel management company is subject to prior review and acceptance by Port Staff and which review shall be conducted by an independent third party, which shall not be unreasonably	No Change
21	Assignment	**Prior to completion of the Project and during the first seven (7) years of the Lease** Tenant may not assign its interest in the LDDA or Lease, as applicable, without the prior written consent of the Port Commission subject to the following: Developer acknowledges that Port is entering into the LDDA and/or Lease on the basis of Developer's special skills, capabilities, and experience. This LDDA and the Lease are personal to Developer and neither may not be Transferred without the Port Commission's prior consent, which consent may not be unreasonably withheld, conditioned or delayed; provided, however, it will be reasonable for Port to	No Change

	Term	Deal Terms as of April 26, 2016	TZK's Proposed changes as of May 22, 2019
		withhold its consent to any assignment or transfer (i) that would result in a change in use of the dinner-theater operations and location and provided Port approves of the change in use, the percentage rent owed to Port from the gross revenues from such new use is less than the percentage rent received by Port for similar uses, or (ii) the initial and subsequent IRR thresholds are not reduced to account for the assignee's or transferee's reduced risk on its investment in the Project.	

Exhibit D

The Development Provides Numerous Benefits to the Public Trust

The proposed lease provides numerous public benefits to the public trust, including (a) new hotel, dinner-theater and other visitor-serving uses that will enhance public use and enjoyment of the waterfront, (b) creation of new public open space, (c) elimination of barriers to the waterfront and uniting the landside with the waterfront, (d) enhanced pedestrian, bicycle and transit access along the Waterfront, and (e) increased rent revenues to the Harbor Fund that will exceed the current and projected revenues from existing parking operations on the Site.

A. Hotel, Dinner-Theater, and Other Visitor-Serving Uses.

The Development will add a new 192-room hotel that will provide new opportunities for visitors to come to San Francisco's historic northern waterfront. All of the rooms will be made available for rent to the public -- no private ownership interest in any of the hotel rooms (fractional ownership or timeshares) will be permitted. The hotel will include a restaurant/café and bar that will be open to the general public, and the hotel lobby will also be open to the public.

The Development also includes a permanent home for Teatro ZinZanni, a unique dinner theater experience that will be a major waterfront attraction. ZinZanni's signature Speigeltent was long associated with the San Francisco waterfront at nearby Piers 27 and 29. The project will revive the Speigeltent and add to the diversity of experiences available on the northern waterfront. Together with the hotel, the dinner theater will attract many visitors to the water and enhance the use and enjoyment of the waterfront by the public.

B. Creation of Public Open Space.

The Development includes a new approximately 14,000 square foot public open space and public access walkways around the entire Development site, a walking path through the public open space and enhancements to The Embarcadero, Broadway and Davis Street streetscapes.

C. Elimination of Barriers to the Waterfront, Uniting the Land Side Neighborhood with the Waterfront, and Promoting Public Access to and along the Waterfront.

The Site is currently used as a surface parking lot along the Embarcadero. Both Vallejo Street and Davis Street terminate on the land side of the Site, inhibiting public access to The Embarcadero and creating a barrier between the waterfront and the rest of the City at this location. The Development includes a pedestrian path from the intersection of Davis Street and Vallejo Street to The Embarcadero along the new public open space, eliminating the existing visual and public access barrier and creating a new, welcoming connection between the waterfront and the land side of the City.

This development is anticipated to create a landmark that highlights the intersection of Broadway and The Embarcadero as a gateway to Chinatown and North Beach, and create an orientation point along the waterfront. It is also anticipated to activate and revitalize the waterfront edge in the Northeast Waterfront area, establishing a daytime and nighttime presence in the area, making the area inviting to local residents as well as visitors and respect and complement the historic and architectural character of the Northeast Waterfront Historic District. These features will further unite and integrate the land side neighborhoods with the waterfront.

D. The Project will promote and enhance pedestrian, bicycle and transit access along the Waterfront.

The Site currently contains no developed public access areas except along the under-utilized sidewalks. The Site, when improved with the Development, will be welcoming to the public through enhanced pedestrian, bicycle and transit access along the waterfront as described below.

The Development will include enhancements along The Embarcadero, Broadway and Davis Street that are consistent with The Embarcadero Streetscape Plan and the other relevant City plans and policies for the area. Bulb-outs and way-finding treatments, consistent with the WLUP, the City's plans and policies, will be constructed, installed and maintained. Class I and Class II bicycle amenities will be constructed and maintained as part of the Development. Moreover, as stated above, one of the many unique features of the Development is the ability of the public to "see behind the scenes of ZinZanni" as a result of the design of the glass gazebo for the historic Speigeltent, which itself has numerous pedestrian improvement to make the experience at the Development public and welcoming with views to the Bay and The Embarcadero.

E. Increased Revenues to Harbor Fund.

The financial terms of the proposed lease provide for a minimum base rent to the Port that exceeds existing and projected revenues from existing parking operations. In addition to the minimum rent, the proposed lease also includes payments to Port from a percentage of the Development's annual gross revenue (when such amount exceeds the minimum base rent), and upon satisfaction of certain conditions, additional payment to Port from a sale of the tenant's leasehold interest or refinancing. Port obtained an appraisal on the fair market value of the Site, which appraisal serves as the basis for the setting the minimum base rent.