

MEMORANDUM

September 2, 2015

TO: MEMBERS, PORT COMMISSION
Hon. Leslie Katz, President
Hon. Willie Adams, Vice President
Hon. Kimberly Brandon
Hon. Doreen Woo Ho

FROM: Monique Moyer
Executive Director

SUBJECT: Request authorization to enter into Exclusive Negotiation Agreement with Teatro ZinZanni and its financial partner, Kenwood Investments No. 6, LLC, operating together as TZK Broadway, LLC, for the lease and development of a dinner-theater and a maximum 200-room, 40-foot high boutique hotel and an approximately 7,500 square foot privately financed public park and ancillary uses at Seawall Lots 323/324 and portions of Vallejo and Davis Street right-of-ways on the west side of The Embarcadero at Vallejo Street

DIRECTOR'S RECOMMENDATION: Approve Attached Resolution

EXECUTIVE SUMMARY

Port staff requests authorization to enter into an Exclusive Negotiation Agreement (“ENA”) with TZK Broadway, LLC (“TZK”), a California limited liability company, for the lease and development of an approximately 200-room hotel, dinner-theater and a public park on the Site (as defined below). This request is based in part on Resolution No. 170-15 that the Board of Supervisors (the “Board”) adopted on May 5, 2015 which, among other things, exempts TZK from the competitive bidding policy set forth in Administrative Code Section 2.6-1 and urges City officials to take all actions needed to negotiate an ENA and a term sheet with TZK.

During the ENA period, Port staff will work with TZK to refine the proposed development concept and negotiate a term sheet covering lease terms that meet the Port’s management obligations. The initial ENA term will be for a one-year period, with four optional six-month extensions, to develop project plans, negotiate a term sheet for required agreements, and secure needed approvals, including Port Commission’s and

THIS PRINT COVERS CALENDAR ITEM NO. 14B

the Board's endorsements of the term sheet prior to drafting full transaction documents that are subject to the respective consideration/approval of the Port Commission and the Board, as applicable. The ENA requires TZK to (i) pay to Port a negotiation fee of \$100,000 and (ii) reimburse Port's costs related to the project during the ENA period.

Port staff recommends the ENA approval.

Port staff last made a presentation to the Port Commission on this proposed development on October 28, 2014. On that date, the Port Commission approved Resolution No. 14-58¹ directing Port staff to assist Teatro in developing and introducing a resolution to the Board to consider exempting the proposed Development from the City's competitive bidding procedures with respect to the potential lease of the Site to Teatro and TZK.

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 to be developed with the two abutting right-of-way parcels ("Paper Streets") that form the terminus of Vallejo Street and Davis Street as they intersect The Embarcadero. The four parcels, SWLs 323 and 324, and the two Paper Streets, have a combined land area of 57,170 square feet and they form the site (the "Site") to be leased for the proposed development. A Site Map is attached as Exhibit A. The Site is currently paved with asphalt, striped for 227 self-parked stalls, and leased on an interim basis to a parking operator, Priority Parking CA, for surface parking lot operation that generated approximately \$1 million in net annual revenue to the Port in fiscal 2014-2015.

Hotel, entertainment, theatre, 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. These lots are subject to the common law public trust doctrine, as well as to the terms and conditions of the Burton Act, which is the trust grant from the State of California to the City (sometimes referred to collectively as the "public trust").

Teatro ZinZanni and Relocation Plan

Teatro is a popular dinner theater performed in a historic Spiegel tent, which provides a big top setting for live music, comedy, and acrobatic entertainment. It is a unique hybrid of comedy, theater, cabaret, music and dining that is part circus and part cabaret. It combines improvisational comedy, vaudeville revue, music, dance and cirque into an evolving form. It operates a venue in Seattle, Washington and operated a venue in San Francisco.

¹ <http://www.sfport.com/modules/showdocument.aspx?documentid=9020>

Teatro and the Port entered into a lease in 1999 for Teatro to use a portion of Piers of 27 and 29 for its dinner theater and cabaret operations (the “Theater Lease”). The Theater 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 on 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, completion of environmental review, etc.), the parties would enter into a new lease for a portion of SWL 324.

On October 28, 2014, the Port Commission approved Resolution No. 14-58 directing Port staff to assist Teatro in developing and introducing a resolution to the Board to consider exempting the proposed Development from the City’s competitive bidding procedures with respect to the potential lease of the Site to Teatro and TZK.

On May 5, 2015, the Board adopted Resolution No. 170-15² (the “Board Resolution”), which found that the proposed Development is exempt from competitive bidding requirements of Administrative Code Section 2.6-1 on the following basis: the unique, one-of-a-kind attributes of Teatro; the unique opportunity presented by Developer’s proposal to build and finance the Development; and Teatro’s position as a tenant in good standing under Port policies; the provisions of the Mutual Termination Agreement; and, in keeping with Administrative Code Chapter 90A to retain an important entertainment icon, provide performer lodging and workforce training, and numerous other public benefits to the City and the region that the proposed Development would produce, as further described in the Board Resolution.

The Board Resolution also (i) urged Port, Teatro and Developer to engage in continued outreach to affected and interested neighbors, community members and stakeholders to ensure that the proposed Development is designed with public input; (ii) urged the Port to hire a third party real estate economic consultant during negotiations with Developer to ensure the Port receives fair market value for the lease of the Site; and (iii) directed Port to submit to the Clerk of the Board (“Clerk”) a copy of Port’s real estate consultant’s report confirming TZK’s qualifications to undertake the development prior to the Port Commission’s hearing at which the Port Commission considers awarding this Agreement to Developer.

Kenwood Investments’ Qualifications and Financial Capacity

In June, Kenwood Investments provided the Port a description of its qualifications and financial capacity. BAE Urban Economics, Port-hired third-party real estate consultant (“BAE”), and Port staff respectively 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 on August 18, 2015 as required.

² <http://www.sfbos.org/ftp/uploadedfiles/bdsupvrs/resolutions15/r0170-15.pdf>

EXCLUSIVE NEGOTIATIONS PROCESS

The ENA is the agreement between the Port and TZK governing how the required development agreements will be negotiated. It establishes time and performance benchmarks, provisions for time extensions to perform and termination for non-performance. It also establishes the time frames and milestones for required Port Commission, Planning Commission, and the Board's review and approval; and specifies negotiation fees payable to Port and recovery of Port's costs associated with the Development.

During the ENA period, the following key events are anticipated to occur:

- TZK will commence and complete its due diligence review of the Site.
- TZK will conduct community outreach to stakeholders.
- Port and TZK will negotiate a term sheet for Port Commission and Board's endorsement.
- TZK will complete preliminary architectural and engineering designs, and finalize financial projections addressing lease payments to the Port, and the equity and debt required to completely finance the entitlement, construction, and operation of the Development.
- TZK will complete any required environmental review and required regulatory approvals.
- The Port and TZK will negotiate as applicable a lease disposition and development agreement, a lease, and related documents for the Development incorporating specific terms, including the Port's and TZK's respective responsibilities, the economic parameters, development standards and requirements, and a performance schedule. The lease is subject to the Port Commission's and Board's approval following the completion of environmental review.

The Port Commission, by approving the ENA is not approving a project, nor committing either party to a project. Rather, the ENA establishes the parameters for consideration of a possible project or development.

SUMMARY OF ENA TERMS

Fee, Term, and Extensions: For the right to exclusively commit Port to negotiate with TZK, the Port imposes a negotiating fee of \$100,000 for the initial term of one-year. TZK can extend the term by four six-month (6-Month) extensions subject to a \$50,000 fee for each extension. TZK will pay half (\$50,000) of the initial term fee during the ENA period and the balance for the initial term fee at the close of the construction loan for the Development. If the construction loan does not close because the Development does not move forward, the \$50,000 balance will not be paid to Port.

Transaction Costs: The ENA provides for TZK to fund Port's costs (including third party costs and staff time) associated with project Planning and review and negotiating transaction documents.

Performance Benchmarks: Exhibit B shows the performance benchmarks and schedules included in the ENA. Review of Exhibit B indicates that the next major step will be consideration of an updated proposal, which will happen in Fall 2015. If TZK is diligently pursuing the benchmarks, it may request an extension of its performance deadlines in accordance with the ENA. This ENA assumes that the Port Commission authorizes the Executive Director or her designee, to waive or extend the times established for attaining the specified performance benchmarks, including the right to condition such waiver or extension on additional terms and conditions or approval from the Port Commission in its sole discretion.

Regulatory Approvals: TZK is responsible for obtaining all regulatory approvals in collaboration with the Port.

Project Material: TZK will assign to Port all studies, applications, reports, permits, plans, drawings and similar non-proprietary work and materials relating to the Development prepared by its consultants, if the ENA is terminated.

RECOMMENDATION

Port staff recommends approval of the ENA for the proposed Development at the Site with TZK Broadway, LLC.

Prepared by: Ricky Tijani
Development Project Manager

For: Byron Rhett, Deputy Director
Planning & Development

Exhibits: A. Site Map
B. Performance Benchmarks

Exhibit A Site Map

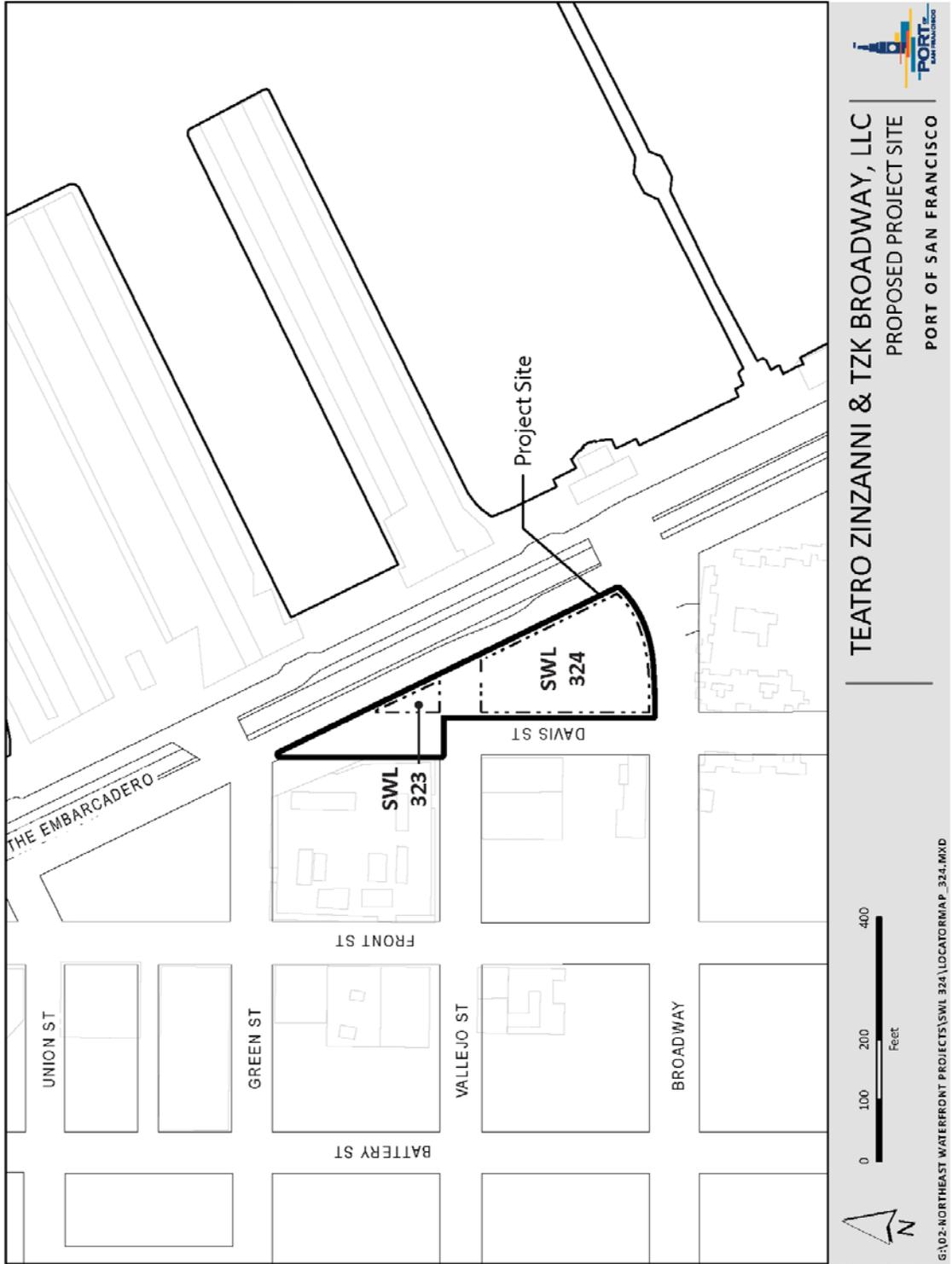


EXHIBIT B
ENA Performance Benchmarks

Performance Benchmarks	Time for Performance
1. <u>Developer Formation Documents</u> : TZK to provide updates to Port if there are any material changes to the documents.	Ongoing
2. <u>Updated Proposed Development Concept</u> : TZK must submit its updated development concept showing its preliminary massing and land use concept.	October 2015
3. <u>Community Outreach Plan</u> : TZK must submit its proposed Community Outreach Plan	October, 2015
4. <u>Public Trust Consistency Proposal</u> : TZK must submit its proposed Public Trust Consistency Plan for the Site	December 2015
5. <u>Deal Term Sheet</u> : TZK must submit its proposed Term Sheet of the Revised Development Proposal. What to cover in Term Sheet: <ul style="list-style-type: none"> 1. Lease terms and conditions including all the terms set forth in Section 3.2 of the ENA. 2. Terms/conditions of related transaction documents 	January 2016
6. <u>Site Control for non-Port Parcels</u> : TZK must submit its plan for Site Control of DPW Street stubs	January 2016
7. <u>Regulatory Approval Strategy</u> : TZK must submit its proposed Regulatory Approval Strategy	January 2016
8. <u>Design Review Submission</u> : TZK must submit its design concept for review by the applicable regulatory bodies	February 2016
9. <u>Port Commission Endorsement</u> : TZK to obtain the Port Commission's endorsement of the Term Sheet	February 2016
10. <u>Board Endorsement and Fiscal Feasibility Determination</u> : TZK to obtain the Board of Supervisors' endorsement of the Term Sheet and if required, Fiscal Feasibility Determination	March 2016
11. <u>Implementation Strategies</u> : Traffic and parking impact mitigation, financing, franchising/branding, building operations, operation management, leasing, and public benefit improvements	September 2015 -- April 2016

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| 12. | <u>CEQA Environmental Evaluation</u> : TZK to submit the environmental evaluation application for the Development with a timeline for the publication of certification of environmental review | September 2015 – April 2016 |
| 13. | <u>Due Diligence Investigation</u> : TZK must complete its due diligence investigation of the Site, including surveys, title, environmental site assessment, field measurements, samples, borings, soil and geotechnical analysis, utility availability, and any other investigations as required by its technical advisors | April 2016 |
| 14. | <u>Transaction Documents</u> : TZK and Port must reach final agreement on the form of LDDA, Lease and all related transaction documents | June 2016 |
| 15. | Port Commission adoption of CEQA Findings and Public Trust Consistency findings, and approval of final Transaction Documents | June 2016 |
| 16. | Board of Supervisors' Adoption of CEQA Findings and Approval of Lease | September 2016 |

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

RESOLUTION NO. 15-31

WHEREAS, Charter Section B3.581 empowers the Port Commission with the authority and duty to use, conduct, operate, maintain, manage, regulate and control the lands within Port jurisdiction; and

WHEREAS, Seawall Lot 323 (“SWL 323”) and Seawall Lot 324 (“SWL 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 (collectively, the “SWLs”) which are to be developed with the two abutting right-of-way parcels that form the terminus of Vallejo Street and Davis Street as they intersect The Embarcadero totaling a combined land area of 57,170 square feet and constituting the site for the proposed Development described in this Resolution (the “Site”); and

WHEREAS, The SWLs are part of the Northeast Waterfront area and hotel, entertainment, theatre and public open space uses are allowed uses in such area under the Port’s Waterfront Land Use Plan, the City Planning Department’s Northeastern Waterfront Subarea Plan, and the Planning Department’s Northeast Embarcadero Study issued in June of 2013; and

WHEREAS, The Site is currently operated as a surface parking lot by Priority Parking CA pursuant to that certain Lease No. L- 14747 dated October 1, 2009; and

WHEREAS, Port and One Reel, a Washington State nonprofit corporation (“Teatro”), entered into that certain Lease No. L-12847 in 1999 (as amended, the “Theater Lease”) for Teatro to use certain portions of Piers 27 and 29 for its dinner theater and cabaret operations named Teatro ZinZanni, which Theater Lease terminated in 2011 pursuant to that certain Mutual Agreement for Lease Termination and Reservation of Rights Agreement dated August 12, 2011 (“Mutual Termination Agreement”); and

WHEREAS, The Port and Teatro identified SWL 324 as a potential relocation site for Teatro ZinZanni in the Mutual Termination Agreement; and

WHEREAS, Teatro is now proposing to develop on all of SWL 324, the adjacent SWL 323, and adjacent right-of-ways (i) a new privately financed theatre for Teatro; and (ii) a boutique hotel with a maximum of 200 rooms, including up to 10 transient residences for visiting Teatro artists, all situated within a 40-foot high, four-story building, together with related public improvements, including a new public park (the “Development” or “Project”); and

- WHEREAS, Teatro has brought on Kenwood Investments specifically for Kenwood Investments' expertise on hotel development and project financing; and
- WHEREAS, TZK, LLC, a California limited liability company ("TZK" or "Developer"), the entity entering into the Exclusive Negotiation Agreement ("ENA") as the developer, is comprised of two members: TZZ, LLC, a Washington State limited liability company, an affiliate of Teatro, and Kenwood Investments No. 6 LLC, an affiliate of Kenwood Investments; and
- WHEREAS, On October 28, 2014, the Port Commission approved Resolution No. 14-58 directing Port staff to assist Teatro in developing and introducing a resolution to the Board of Supervisors ("Board") to consider exempting the potential lease of the Site for the proposed Development from the City's competitive bidding policy set forth in Administrative Code Section 2.6-1; and
- WHEREAS, On May 5, 2015, the Board adopted Resolution No. 170-15 (the "Board Resolution"), which found that the proposed Development is exempt from competitive bidding requirements of Administrative Code Section 2.6-1 on the following basis: the unique, one-of-a-kind attributes of Teatro; the unique opportunity presented by Developer's proposal to build and finance the Project; Teatro's position as a tenant in good standing under Port policies; the provisions of the Mutual Termination Agreement; and, in keeping with Administrative Code Chapter 90A to retain an important entertainment icon, provide performer lodging and workforce training, and numerous other public benefits to the City and the region that the proposed Project would produce, as further described in the Board Resolution; and
- WHEREAS, The Board Resolution also (i) urged Port, Teatro and Developer to engage in continued outreach to affected and interested neighbors, community members and stakeholders to ensure that the proposed Development is designed with public input; (ii) urged Port to hire a third party real estate economic consultant during negotiations with Developer to ensure Port receive fair market value for the lease of the Site; and (iii) directed Port to submit to the Clerk of the Board a copy of Port's real estate consultant's report confirming TZK's qualifications to undertake the development prior to the Port Commission hearing at which the Port Commission considers awarding an ENA to Developer; and
- WHEREAS, In June 2015, Kenwood Investments provided the Port a description of its qualifications and financial capacity which BAE Urban Economics, Port-hired third-party real estate consultant ("BAE"), and Port staff respectively reviewed, with BAE issuing a report confirming that Kenwood Investments is qualified to develop the Project and which report the Port submitted to the Clerk of the Board on August 18, 2015; and

WHEREAS, The Port Commission has reviewed the Board Resolution and has reviewed Port staff recommendations set forth in the Staff Report accompanying this resolution, and has determined that the Port should enter into the ENA with TZK; now, therefore, be it

RESOLVED, That the Port Commission authorizes the Executive Director of the Port (“Executive Director”) or her designee to execute the ENA and any additions, amendments or other modifications thereto that are necessary and advisable to complete the ENA consistent with the terms and conditions set forth in the Staff Memorandum and in a form approved by the City Attorney which key terms and conditions of the ENA include, in summary: (i) a \$100,000 negotiation fee for the one-year initial term with \$50,000 due during the ENA period and the balance at the Development’s construction loan closing, (ii) four six-month extension options each subject to a \$50,000 fee, (iii) TZK responsible for all of Port’s transaction costs related to the Development, (iv) TZK responsible for obtaining all regulatory approvals, and (v) assignment to Port of all project studies, applications, reports, permits, plans, drawings, and similar non-proprietary work and materials prepared by its consultants upon termination of the ENA; and, be it further

RESOLVED, That Port staff engage a third party real estate economic consultant during negotiations with Developer to ensure Port receive fair market value for the lease of the Site; and, be it further

RESOLVED, That the Port Commission hereby authorizes the Executive Director or her designee, to waive or extend the times established in the ENA for attaining the specified performance benchmarks attached to the Staff Memorandum accompanying this resolution as Exhibit B, including the right to condition such waiver or extension on additional terms and conditions or approval from the Port Commission in its sole discretion; and be it further

RESOLVED, That the Port Commission reserves the right, if negotiations with TZK are unsuccessful and do not lead to approval of a development agreement, lease and related documents, or if the ENA is terminated before expiration of its term, to undertake other efforts, which may include selecting a developer/tenant by any other means, or issuing a developer solicitation, all in the Port Commission’s sole discretion; and, be it further

RESOLVED, That entering into the ENA with TZK begins a process of refining the scope of its development for the Site, and that TZK’s proposal will evolve through the public review process, all leading to a final development proposal to be submitted to the Port Commission for review and approval; and, be it further

RESOLVED, That the ENA does not commit the Port Commission to approval of any specific development concept or project proposal, nor does the ENA foreclose the possibility of alternative development concepts, mitigation measures, or deciding not to grant entitlements or approve the lease and development of the proposed concept; and, be it further

RESOLVED, That entering into exclusive negotiations does not commit the Port Commission to approval of a final lease or related documents and that the Port Commission shall not take any discretionary actions committing it to the Development until it has reviewed and considered environmental documentation prepared in compliance with the California Environmental Quality Act.

I hereby certify that the foregoing resolution was adopted by the Port Commission at its meeting of September 8, 2015.

Secretary