MEMORANDUM

March 7, 2013

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

FROM: Monique Moyer
    Executive Director

SUBJECT: Request authorization to amend the Exclusive Negotiation Agreement with Orton Development, Inc. for the lease and rehabilitation of the 20th Street Historic Buildings on or near 20th and Illinois Streets at Pier 70

DIRECTOR’S RECOMMENDATION: Approve Attached Resolution

EXECUTIVE SUMMARY

This memorandum describes proposed changes to the terms of the Exclusive Negotiation Agreement (“ENA”), dated as of May 16, 2012, between Orton Development Inc. (“ODI”) and the Port for the rights to lease, rehabilitate and operate six historic buildings (the “Project”) included in the Pier 70 Master Plan area and shown as the Historic Core on Exhibit A. On April 24, 2012, the Port Commission authorized the Executive Director to execute this ENA. On October 9, 2012, the Port Commission endorsed the Term Sheet establishing the conceptual agreement by the parties of the terms of a transaction to realize the Project.

Two changes to the ENA are proposed:
• Revise the termination date of the ENA to December 20, 2013, adding ten months to the existing nine-month term that ended on February 19, 2013.
• Revise ODI’s financial obligation to reimburse the Port for its transaction costs.

THIS PRINT COVERS CALENDAR ITEM NO. 10D

1 Background on Term Sheet as well as the land use planning, competitive solicitation, and ENA authorization prior to the Term Sheet with ODI, are discussed in Item 9C on the October 9, 2012 agenda: http://www.sfport.com/index.aspx?page=2132
BACKGROUND

The Pier 70 Master Plan area\(^2\) includes 69 acres of land roughly bounded by Mariposa, Illinois, and 22\(^{nd}\) Streets and the San Francisco Bay. The 20\(^{th}\) Street Historic Buildings are six buildings on or near 20\(^{th}\) Street at Pier 70. These historic resources, some dating to the 1880s, are in need of substantial investment to return to active use with some estimates at well over $100 million. The condition of the buildings, the nature of a ground lease transaction, the lack of infrastructure services, and the transitional state of the overall Pier 70 area combine to make this a challenging real estate project.

On February 28, 2012, the Port selected ODI as its development partner for these buildings. Following due diligence and negotiation, the Port and ODI agreed to the Term Sheet endorsed late 2012. ODI has defined a use program of office, light industrial and commercial uses\(^3\) that can revitalize these buildings and has estimated a capital cost of $58 million. The basic terms of the transaction are that ODI will rehabilitate these buildings, including securing needed investment, in exchange for a 66 year lease and a $1.5 million capital contribution from the Port.

Revenues from the Project will first fund operating costs, then debt service and, until ODI’s equity is recovered, ODI will receive a 14\% percent return (on a simple interest basis) on its investment. ODI and the Port will share equally in net cash flow after ODI’s equity is repaid. An annual guaranteed base rent of $200,000 (escalated to reflect inflation) is due 20 years after commencement of the lease. The terms proposed provide the Port a means to share in the upside of the project yet catalyze the project by deferring guaranteed base rent for 20 years.

CERTAIN EXISTING ENA TERMS

As authorized by the Port Commission on April 24, 2012, the Port and ODI entered into the ENA. The ENA is the agreement between the parties establishing the parameters for consideration of a possible rehabilitation project. The ENA establishes time and performance benchmarks including provisions for extensions and termination for non-performance. The existing ENA has a nine-month term to secure Port Commission and Board of Supervisors’ approval of applicable Transaction Documents. Additionally, the ENA requires ODI to fund Port's costs (including third party costs and staff time) associated with the Project, including, but not limited to Project review and negotiating Transaction Documents. To date, ODI has paid $80,000 toward Port transaction costs.

Late last year, the Port and ODI reached an important milestone by securing Port Commission and Board of Supervisors endorsement of the Term Sheet and the Board of

\(^2\) On September 25, 2012, the Port Commission received a comprehensive briefing on the Port's progress on implementation of the Pier 70 Master Plan; the Staff Report is Item 9B on this agenda: [http://www.sfport.com/index.aspx?page=2128](http://www.sfport.com/index.aspx?page=2128)

\(^3\) ODI’s concept includes replacing building systems, repair and maintenance, seismic and structural upgrades, security measures, and abatement of hazardous environmental conditions. All work will be consistent with the Secretary of the Interior’s Standards for the Treatment of Historic Properties. Proposed uses by building are:

- Building 101 and 104 will return to office use
- The Building 101 former cafeteria will remain food production and Building 102 will become a restaurant.
- The Union Ironworks Machine shop (Building 113) and surrounding warehouses (Buildings 114/115/116 and Building 14) will return to industrial use with ancillary office and retail.
Supervisors finding the Project fiscally feasible. ODI has also undertaken extensive investigations of the buildings and is close to completing construction drawings for the Project. Actions yet to occur in the ENA period include:

- Completion of required environmental review
- Completion of due diligence review of the site, finalization of financial projections, and completion of rehabilitation plans
- Negotiation of the lease disposition and development agreement (LDDA), lease and other transaction documents.
- Port Commission and Board of Supervisors approval of the applicable Transaction Documents.

RECOMMENDED ENA CHANGES

Term

The ENA was scheduled to terminate on February 19, 2013. ODI requested a short, force majeure extension, as the original nine-month ENA term did not anticipate the need to secure Board of Supervisors' finding of project fiscal feasibility prior to commencing CEQA review. The ENA provides for a regulatory force majeure extension of the ENA term if the Developer is unable to satisfy any Performance Benchmark because of a delay that is both reasonably outside of Developer’s control and likely to prevent the parties from timely entering into the Transaction Documents. Port staff concurred that the need to secure fiscal feasibility approval added six weeks to the timeframe for approvals and agreed to extend the ENA term until March 31, 2013. Port staff recommends lengthening the initial ENA term further to allow sufficient time for Project review and approvals. The amendment proposed, and the new performance benchmarks shown in Exhibit B, will extend the ENA term to December 20, 2013, if approved by the Port Commission. This proposed ENA amendment will provide the time needed to complete the Project review and negotiate the Transaction Documents. As discussed above, ODI has undertaken engineering and design work that can allow construction to commence soon after transaction approvals.

ODI will continue to have the right, for a $50,000 fee for each extension, to extend the ENA twice by ODI for six months each. If exercised, these extensions allow for a potential ENA term ending on December 20, 2014.

Transaction Costs

To be consistent with the participating rent structure agreed to in the Term Sheet, Staff recommends revising the transaction cost recovery terms of the ENA. During the ENA term, Port Staff recommends capping ODI’s obligation to reimburse the Port for its transaction costs at the $80,000 paid through the end of 2012. Through the end of 2012, the Port Transaction costs including legal and consulting fees were $160,000.

With this amendment, reimbursement to the Port for its transaction costs in excess of $80,000 will be deferred until Project revenues can support repayment on par with payments to ODI, which obligations will be further refined in the Lease. Deferring ODI’s

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4 The regulatory force majeure provisions of the ENA (Section 2.2) do not require Port Commission approval of such extensions. The ENA allows one or more Regulatory Force Majeure Extensions of no more than 6 months in the aggregate upon written notice.
reimbursement obligation reduces the Project front-end costs and lowers the required equity investment that would accrue at a 14% return. If the Project does not occur, the Port will not be reimbursed for transaction costs above the $80,000 received to date. Port transaction costs are estimated to be $250,000 through the execution of the LDDA anticipated at year end of 2013.

**NEXT STEPS**
The Port and ODI will continue the Project review and analysis necessary to negotiate and obtain approval for the LDDA and Lease for the Project by the Port Commission and the Board of Supervisors. Throughout this process, there will be numerous opportunities for public comment and review of the proposed project. Approvals for the project are anticipated to occur in late 2013 with construction to commence soon after.

**RECOMMENDATION**
Extending the ODI ENA term and revising the transaction cost recovery mechanism are important and necessary steps in the rehabilitation of the 20th Street Historic Buildings at Pier 70. Port Staff respectfully request approval of the amendments to the ENA, as described above, to provide sufficient time to complete negotiations and review and to align the transaction costs recovery mechanism with the Term Sheet approved in late 2012.

Prepared by: Kathleen Diohep, Manager
Public/Private Development Projects

Through: Jonathan Stern, Assistant Deputy Director Waterfront Development

For: Byron Rhett, Deputy Director Planning & Development

Exhibits
A. Location Map
B. Performance Benchmarks
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, On or near 20th Street, east of Illinois Street, the Port owns a cluster of historic buildings in need of substantial rehabilitation (the “20th Street Historic Buildings”), which, if adaptively reused, would create an extraordinary showcase for Pier 70’s heritage; and

WHEREAS, On February 28, 2012, by Resolution No. 12-18, the Port Commission awarded Orton Development Inc. (“ODI”) an exclusive right to negotiate with the Port for the development, rehabilitation, and lease of the 20th Street Historic Buildings (“the Project”); and

WHEREAS, On April 24, 2012, by Resolution No.12-36, the Port Commission authorized the Executive Director or her designee to execute an Exclusive Negotiating Agreement (“ENA”) between the Port and ODI for the Project and the Port and ODI entered into the ENA effective May 17, 2012; and

WHEREAS, On October 9, 2012, by Resolution No. 12-78, the Port Commission endorsed the term sheet for the Project (“Term Sheet”) and on December 4, 2012, the San Francisco Board of Supervisors, by Resolution 440-12, endorsed the Term Sheet and found that the Project is fiscally feasible and responsible under San Francisco Administrative Code Chapter 29; and

WHEREAS, The Project is more complex than initially anticipated and as a result the parties have not been able to finalize negotiation of the Transaction Documents and ODI has not yet been able to submit the CEQA environmental evaluation application for the Project to the Planning Department, extending the ENA termination date to December 20, 2013 provides sufficient time to complete the performance benchmarks; and

WHEREAS, Port’s transaction costs incurred pursuant to the ENA that are reimbursed by ODI, under the Term Sheet agreed to by the parties, are considered equity investment in the Project by ODI and will accrue a 14% return on all outstanding balances, thus amending the ENA to defer a portion of the Port’s transaction costs until Project revenues can support repayment on par with payments to ODI, to be further refined in the lease for the project site, reduces the Project front-end costs and lowers the required equity investment that would accrue at a 14% return; and

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WHEREAS, The Port Commission recognizes that deferring recovery of Port transaction costs greater than $80,000 until such costs can be repaid from Project revenue only provides for recovery of such costs if the Project is realized; now. therefore be it

RESOLVED, That the Port Commission authorizes amending the ENA to extend the initial termination date to December 20, 2013 and to defer payment of Port transaction costs over $80,000 until the Project revenues support repayment on par with developer cost recovery; and, be it further

RESOLVED, That the Port Commission authorizes the Executive Director or her designee to execute the First Amendment to the ENA and any additions, amendments or other modifications thereto that are necessary and advisable consistent with the terms and conditions set forth in the Staff Memorandum accompanying this resolution and in a form approved by the City Attorney; and, be it further

RESOLVED, That the Port Commission hereby authorizes the Executive Director of the Port, or her designee, to waive or extend the times established in the ENA for performance of specific objectives under the ENA as specified in the ENA, including the right to condition such waiver or extension on additional performance objectives or other conditions required by the Port Commission in its sole discretion; and, be it further

RESOLVED, That amending the ENA does not commit the Port Commission or the City to approval of final Transaction Documents or implementation of the Project or grant any entitlements to ODI, nor foreclose the possibility of considering alternatives to the proposal, mitigation measures or deciding not to grant entitlement or approve or implement the Project, after conducting appropriate environmental review under CEQA; and, be it further

RESOLVED, That the Port Commission will not take any discretionary actions committing the Port to implement the Project, and the provisions of the ENA are not intended and will not become contractually binding on the Port unless and until the Port Commission has reviewed and considered environmental documentation prepared in compliance with CEQA for the Project and the Port Commission, and as applicable, the Board of Supervisors and the Mayor, have approved final Transaction Documents for the Project.

I hereby certify that the foregoing resolution was adopted by the Port Commission at its meeting of March 12, 2013.

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Secretary
EXHIBIT A: PIER 70 PROJECTS

PIER 70 PROJECT SUB AREAS

* NOTE: BOUNDARIES BETWEEN PROJECT ARE CONCEPTUAL AND MAY SLIGHTLY VARY FROM THE EXCLUSIVE ACCESS/USE AGREEMENT EXCEPT AS NOTED IN DETAILS ARE NEGOTIATED.

SEPTEMBER 2012

C:\05-Southern Waterfront\PIER 70\Master Plan\Graphics\April 2010 Plan Maps\PDF Maps (for print)\PIER70_Exhibit A+v.1.9-20.pdf
## Exhibit B

### ENA Performance Benchmarks

<table>
<thead>
<tr>
<th>Performance Benchmarks</th>
<th>Time for Performance</th>
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<tbody>
<tr>
<td>1. Community Outreach Plan</td>
<td>Completed</td>
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<tr>
<td>2. Project Description</td>
<td>Completed</td>
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<tr>
<td>3. Term Sheet Proposal</td>
<td>Completed</td>
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<td>4. Conceptual Design Review Submission</td>
<td>Completed</td>
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<tr>
<td>5. <strong>Port Commission Endorsement:</strong> Port Commission to adopt a resolution endorsing the Term Sheet</td>
<td>Completed</td>
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<td>6. <strong>Board Endorsements:</strong> Board to endorse the Term Sheet and make Fiscal Feasibility findings</td>
<td>Completed</td>
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### Items to Complete

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<tr>
<th>Performance Benchmarks</th>
<th>Time for Performance</th>
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<tr>
<td>7. <strong>Schematic Designs for Rehabilitation and Public Realm Submission</strong></td>
<td>5/1/2013</td>
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<td>Revised from 8/1/2012</td>
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<td>8. <strong>CEQA Environmental Evaluation:</strong> Submit the environmental evaluation application for the Project</td>
<td>6/15/2013</td>
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<td>Revised from 8/15/2012</td>
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<td>Revised from 9/1/2012</td>
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<td>10. <strong>Full Underwriting Package Submission</strong></td>
<td>6/15/2013</td>
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<td>Revised from 9/1/2012</td>
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<td>12. <strong>Final Transaction Documents:</strong> Developer and Port must reach final agreement on the form of LDDA, Lease and all related transaction documents (including developer entity)</td>
<td>9/1/2013</td>
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<td>13. <strong>Approval of Final Transaction Documents:</strong> Port Commission to adopt Public Trust consistency findings, make CEQA findings and approve final Transaction Documents</td>
<td>10/15/2013</td>
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<td>14. <strong>Board of Supervisor Approvals:</strong> Board to approve Lease as required.</td>
<td>Before 12/20/2013</td>
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