

REPORT

DATE ISSUED: March 2, 2007

REPORT NO: HCR07-26

ATTENTION: Chair and Members of the Housing Commission
For the Agenda of March 23, 2007

SUBJECT: Starbucks Coffee - Smart Corner Leasing Arrangements

REQUESTED ACTION:

Approval by the Housing Commission and the Housing Authority of the proposed leasing arrangement between the San Diego Housing Commission and Starbucks Corporation (“Starbucks”) to lease space at the Smart Corner building.

STAFF RECOMMENDATION:

That the President & Chief Executive Officer (CEO) be authorized to execute lease documents between the Housing Commission and Starbucks, for retail space at the Smart Corner building located at 1122 Broadway, on terms set forth in this report and Attachment 1 and in a lease form as approved by General Counsel to the Commission. The lease would have a ten-year initial term and four 5-year options to renew.

BACKGROUND:

On July 23, 2003 and July 29, 2003 the Housing Commission and the Housing Authority, respectively, approved a Purchase and Sale Agreement (PSA) between the Housing Commission and Lankford & Associates, Inc., for the Housing Commission’s new office facility to be located at 1122 Broadway in San Diego. Further, the Housing Authority delegated responsibility for all cardinal issues related to the acquisition of the office facility to the Housing Commission.

On November 1, 2006, the Housing Commission took title to the parking garage and office building on time and on budget. The Housing Commission occupies three of the five floors in the Smart Corner building. The ground floor is available for lease to retail businesses and the second floor is available for lease to other organizations. The Housing Commission retained the leasing services of CB Richard Ellis to negotiate leasing arrangements with potential tenants.

DISCUSSION:

Attachment 1 is a term sheet for the proposed lease between the San Diego Housing Commission (“Landlord”) and Starbucks (“Tenant”), a Washington corporation. Starbucks will lease approximately 1,825 square feet of space on the first floor of the Smart Corner building located at 1122 Broadway in San Diego. The initial term of the lease will be for ten (10) years; the lease includes four successive options to extend the term of the lease for five (5) years for each option for a total potential lease term of thirty (30) years.

The per square foot (P.S.F.) rent for the first three (3) years of the lease term will be \$3.25 (on a triple net basis), equaling a monthly rent of \$5,931.25 (\$71,175.00 annually). During years four and five (4-5) the rent P.S.F. increases by \$.35 to \$3.60 for a monthly rent of \$6,570.00 (\$78,840.00 annually). In years six to ten the rent increases by another \$.35 p.s.f. to \$3.95 with a monthly rent of \$7,208.75 (\$86,505.00 annually).

Each 5 year option includes an increase in rent culminating with a monthly rent of \$10,256.50 (\$5.62 P.S.F. or \$123,078.00 annually) for years 26 through 30. Taking into account the tenant improvement allowance (monies paid by the Housing Commission to Starbucks in the amount of \$160,123 upon completion of the work by Starbucks) and amortizing the cost over the ten years of the initial lease term equates to a rent of \$2.49 P.S.F. This compares favorably to the original project pro forma rent of \$2.00 per square foot. Space is being rented on a "triple net" basis, meaning that, in addition to rent, Tenant will also pay a share of the ongoing operating costs of the building (janitorial service, utilities, taxes).

Starbucks is required to provide commercial general public liability and property damage insurance of not less than \$2,000,000 per single occurrence and the Housing Commission and the Housing Authority of the City of San Diego will be named as additional insureds (with cross liability endorsements).

The lease allows Starbucks the use of up to 5 parking spaces for employees at an initial rate of \$125 per month.

The proposed lease terms have been negotiated by CB Richard Ellis and Housing Commission staff and the form of lease will be as approved by General Counsel to the Housing Commission. The Commission is requesting that the authority approve the form of the lease, provided that it meets the deal points outlined in Attachment 1 be delegated to the CEO and the General Counsel of the Commission.

FISCAL CONSIDERATIONS:

Funding for the tenant improvement allowance payment to Starbucks of \$160,123 is included in the FY07 Housing Commission budget previously approved by the Housing Commission on April 14, 2006 and the Housing Authority on May 2, 2006.

ENVIRONMENTAL REVIEW: This action is categorically exempt from the provisions of CEQA pursuant to State CEQA Article 19 Guidelines, Section 15301 (existing facilities).

Respectfully submitted,



Steven Snyder
Director, Facilities

Approved by,



Elizabeth C. Morris
President & Chief Executive Officer

DEAL POINTS SUMMARY

FOR THE PROPOSED STARBUCKS LEASE AT SMART CORNER

- Tenant. Starbucks Corporation
- Location. Approximately 1,825 square feet at the northwest corner of the Smart Corner Office Building.
- Use. Tenant may use and occupy the space for (a) a coffee store or (b) any other lawful retail or restaurant use which does not conflict with the written exclusive use presently granted to 7-11.
- Lease Term. 10 Years
- Options. 4 Consecutive 5-Year Options exercisable by Tenant
- Tenant Improvements Allowance. The Tenant is required to construct all of the Tenant Improvements, including improvements the cost of which would normally be borne by the Landlord with an estimated value of \$50,187.50. A Tenant Improvements allowance of \$160,123 is being provided by Landlord, which will be paid by Landlord to Tenant upon completion of the tenant improvements.

- Lease Payments.

<u>Years</u>	<u>P.S.F.</u>	<u>Monthly</u>	<u>Yearly</u>
1-3	\$3.25*	\$5,931.25*	\$71,175.00*
4-5	\$3.60*	\$6,570.00*	\$78,840.00*
6-10	\$3.95*	\$7,208.75*	\$86,505.00*
Extension Options:			
11-15	\$4.00	\$7,300.00	\$87,600.00
16-20	\$4.48	\$8,176.00	\$98,112.00
21-25	\$5.02	\$9,161.50	\$109,938.00
26-30	\$5.62	\$10,256.50	\$123,078.00

*The tenant improvements allowance paid by Landlord to Tenant in excess of that which would normally be borne by the Landlord when amortized over the ten years of the initial lease term equates to an initial rent of \$2.49 P.S.F. for the first 3 years of the Lease, which exceeds the project pro forma rent of \$2.00 per square foot.

- Triple Net Lease. The Lease is triple net to the Landlord, which means that in addition to the rent, Tenant pays a portion of the expenses attributable to operating the ground floor retail portion of the building.
- Tenant Termination Right. The Tenant has the right to terminate the lease after 5-years, by paying \$50,000 to the Landlord.
- Assignment and Subletting. Tenant cannot sublease the space without Landlord's consent, unless the Lease is to (a) a parent, subsidiary, affiliate, division or other entity controlling, controlled by, or under common control with Tenant; (b) a successor entity related to Tenant by merger, consolidation, reorganization or government action; or (c) any entity that engages in a lawful retail or restaurant use. In such event Tenant will remain liable for financial performance pursuant to the Lease and Landlord will be entitled to receive fifty percent (50%) of all "Profit" from such sublease. Notwithstanding the foregoing, the space may not be used for any industrial use, operation of a massage parlor, adult entertainment or adult book store or any similar use,

or for the sale or exhibition of adult or pornographic material, or by tenants that create undue noises, litter or odor, or for a tavern, bar, cocktail lounge (but this shall not prevent the incidental of liquor for on-premises consumption as part of a sit-down restaurant otherwise permitted), or for a skating rink, billiard parlor, bowling alley, school or similar operation or any other use that Landlord reasonably objects to.

- Outdoor Patio. Tenant intends to use the outdoor area immediately adjacent and to the north of the space as an outdoor patio. A temporary emergency staircase to the parking garage is currently occupying the space where the patio is intended to be located. In the event that the temporary emergency staircase is not removed by June 1, 2007, Tenant will be entitled to liquidated damages of \$200 day. The builder/developer of the building is contractually obligated to have the temporary emergency staircase removed by that date.
- Permit Contingency. Tenant has the right to terminate the Lease if it is unable to obtain all permits and governmental approvals needed for the lawful construction and operation of its store within sixty (60) days after execution of the Lease.