PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
ACTION ITEM

Item No. 6e

Date of Meeting November 25, 2014

DATE: November 10, 2014

TO: Ted Fick, Chief Executive Officer

FROM: James R. Schone, Director, Aviation Business Development
Deanna Zachrisson, Business Leader, Airport Dining and Retail

SUBJECT: Authorization of Prime Lease Modification – Anton Airfoods for Anthony's Restaurant operated by HMSHost

ACTION REQUESTED

Request Commission authorization for the Chief Executive Officer to execute an amendment to the lease and concession agreement with Anton Airfoods (operated by Host International/HMSHost) for an additional two years and three months under modified terms and conditions. The draft lease amendment is attached, substantially as drafted (Exhibit B).

SYNOPSIS

In order to facilitate a smooth transition of leases and concepts in the Central Terminal between 2015 and 2017, Airport staff proposes a two-year and three month extension of the lease and concession agreement for Anthony's Restaurant which occupies 7,000 square feet of space on the north side of the Central Terminal and is operated under license agreement by Host International (Host). The current lease length is 10 years from the start of operations, and under the proposed amendment the agreement would terminate on September 30, 2017. This extended time of operation would assure: 1) the continued availability of food service during the same time that other nearby food locations are impacted by construction; and 2) an uninterrupted revenue stream to the Port. In addition, the percentage rent structure for the extension period would be modified and result in increased revenue to the Port. In 2013, Anthony's generated more than $1 million in revenue. Additionally, the extension provides employment stability for approximately 140 employees.

BACKGROUND

In 2000, the Port conducted a Request for Qualifications (RFQ) process in order to lease a newly constructed space on the north side of the Central Terminal. Initially, there were three proposers that responded to the RFQ. The opportunity was first awarded to locally owned Anthony's Restaurants. However, execution of the agreement, the first awardee withdrew from consideration. The second candidate, Anton Airfoods, was chosen to operate a McCormick and Schmick's restaurant under a license agreement. Shortly thereafter, McCormick and Schmick's withdrew their interest in operating in airports. Anton Airfoods proposed a new arrangement for the operation as an Anthony's Restaurant under license agreement with the locally owned company. The Port Commission approved the lease agreement in January 2003 and the restaurant opened for business in June 2005. However, already a month before opening, Anton Airfoods was sold in its entirety and the lease agreement was assigned to the purchaser, Host. Since that time, Host has operated the restaurant.

The RFQ process sought an operator willing to make a significant investment in the Central Terminal space for an initial term of 10-years. With uncertainty about the investment required, and due to the perceived risk of a location without close proximity to gates, the Port also agreed to two 5-year lease options at the Port's sole discretion. Anton Airfoods/Host invested $4.2 million in the initial build out of the restaurant, and another $400,000 in refurbishment in 2010. At the time, the initial investment was the largest investment in a single restaurant in any U.S. airport. All of the initial proposers offered the Port 8% percentage rent on all categories of sales, and this became the negotiated rent in the lease and concession agreement. When the lease agreement was approved in 2003, the Port's development consultant at the time predicted that the Anthony's location would achieve sales of between $4.2 and $4.3 million annually, and provide the Port with approximately $340-$360,000 in annual revenue. Anthony's has been a success far beyond expectations as it achieved sales in calendar year 2013 of more than $13.5 million and generated more than $1 million in Port revenue.

The current lease and concession agreement expires on June 30, 2015, and absent other action, the lease becomes a month-to-month agreement with 30 days' notice to terminate in accordance with the "hold over" provision in the lease. It is unlikely that Host would cease operations in the space; however, because of the large square footage, volume of business and its revenue importance, the Port should not risk the possibility of closure under the hold over provision. It is also important to be assured of continued operations during a period of anticipated construction impacts to other parts of the Central Terminal. Therefore, staff is proposing an extension of the agreement through the summer travel season of 2017. Staff recommends this action rather than the exercise of the existing five-year option. In accordance with the program's phasing plan, the location would be offered in a new competitive RFP process in 2017, to re-open with a possible new concept or operator after completed renovations in 2018.

Currently, nearly all of the leases for the Central Terminal food service locations expire in May-June 2015, which is 10 years after they opened. While it is not a problem to open multiple businesses in an airport simultaneously, it is very problematic to transition their leases simultaneously 10 years later. It is also unwise to disturb business activity during the summer travel season, when the Port and its dining and retail businesses do 30% of their annual sales. As a result, the phasing plan must result in some locations transitioning sooner than others and none during peak travel periods.

The current phasing plan entails the closing of two quick serve units on the south side of the Central Terminal in September 2015. At that time, the current grease duct venting system (which has previously been plagued with operational problems) will be removed from these units, and they will be reconfigured to serve both passengers and future employees in the units more efficiently. The closure of these units will result in a reduction in capacity until they re-open. Upon the completion of those renovations, the remaining quick serve units will be impacted by removal and replacement of the rest of the grease duct venting system as well as by space reconfiguration. The Airport plans to have full capacity of the south side of the Central Terminal restored before the summer of 2017. During the time of the closure impacts, it is important to retain other food service wherever possible. The continued operation of Anthony's is not only possible; it is a preferred option and a logical solution to food service capacity issues.

Anthony's is a one-of-a-kind restaurant in the Airport. It is the only restaurant that provides customers with porcelain tableware, stainless cutlery (including a TSA-approved knife) and cloth napkins. It offers also a full menu reflective of the menus offered at the local street-side counterparts (Anthony's and Chinook's). Staff understands that the costs to operate Anthony's to the quality standards customers expect are very high. Nonetheless, staff believes that a competitive tender of the restaurant location is likely to generate higher percentage rent offers in the future. For this reason, staff believes that it is in the best interest of the Port to not execute one of the available five-year options, but rather undertake a new competitive process in 2017 when the Airport will be better situated operationally and with sufficient food service capacity to transition the restaurant. Even if the incumbent operator were to retain the restaurant space, the Airport can expect that the restaurant will close for some period of time for renovations in late 2017.

REQUEST JUSTIFICATION AND DETAILS

Approval of this lease amendment will allow the Port to sustain adequate food service in the Central Terminal during periods of construction activity. A new competitive process for the restaurant in 2017 will assure that the Port garners the highest possible rent for the 10-year period following. The restaurant operation will sustain approximately 140 management and non-management jobs.

FINANCIAL IMPLICATIONS

As part of the negotiations with Host for this proposed term extension, the company has agreed to a modified rent structure, pending and contingent upon approval by the Host Board of Directors. Currently, as stated above, Host pays 8% of all gross sales in rent to the Port. The new proposed rent structure would be as follows:

Tier	Percentage
0 - $5 million	8%
$5,000,001 - $10 million	10%
Sales over $10,000,001	12%

To place this rent into context, below is the actual rent that Host paid to the Port in the 2013-2014 lease year (July-June), and the rent Host would have paid the Port according to the current proposal. The lease year for Anthony's under the extended term would begin on July 1, 2015 and the new rent structure would commence on that date.

Rent Comparison – Anthony's Restaurant	
2013-2014 Actual Rent	$1,074,095
2013-2014 Illustrative Rent (under new structure)	$1,311,142

The proposed new rent structure will increase Port revenues for the term of the extension through September 2017.

STRATEGIES AND OBJECTIVES:

This project support the Port's Century Agenda goal to "advance the region as a leading tourism and business gateway" by providing an extraordinary customer experience at the Airport. The project also supports the Aviation Division's strategic goals to operate a world-class airport and grow non-aeronautical revenues.

TRIPLE BOTTOM LINE

The Airport Dining and Retail program places a high value on the concurrent pursuit of positive economic, community, customer service and environmental outcomes in management of the program. The proposed extended lease term for Anthony's is clearly consistent with these values.

Economic Development

The extension of the Anthony's operation will lead to increased revenues over those generated today. The amended lease and concession agreement will generate approximately an additional $600,000 in Port revenues. In addition, the Anthony's operation supports approximately 140 full-time jobs with Host (see also below).

Environmental Responsibility

Airport restaurant locations are built to the strictest of Port standards for environmental sustainability with includes durable materials that can withstand high traffic volumes without the need for frequent replacement.

Community Benefits

This proposal supports the continuity of approximately 140 employees with Host. The employees are represented by the Hotel Employees Restaurant Employees union (UniteHERE!) Local 8. Anthony's employee wages are included in a separate wage scale and are generally higher than other Host employees. Starting wages in 2015 will range from $9.44 for tipped servers to $14.94 for a Cook I. The collective bargaining agreement contains annual raises between 5 and 13 cents depending upon type of job classification (non-tipped, tipped and bartender). In addition, employees have access to family health care benefits at a very minimal cost to the employee ($40 or $50 a month depending on tenure). Host contributes $5.09 per hour for each employee to union benefit plans. Host pays an additional 62 cents per hour for pension for each employee. As of January 2015, the lowest wage and benefit rate paid to any Host employee is $15.15 (server category, not including tips). These jobs meet all of the criteria for quality jobs as recently articulated by the Commission.

ALTERNATIVES AND IMPLICATIONS CONSIDERED

Alternative 1) – Allow the lease to move into hold over status while an RFP process is conducted. Issuance of an RFP for the Anthony's location has been unrealistic during 2014, due to the uncertainty associated with the public discourse on minimum wages in SeaTac, Seattle and at the Airport. If the Port issues an RFP in early 2015, the process would not be complete in time for the expiration of the lease in June 2015. The lease would automatically move into hold over status. While it is unlikely that Host would cease to operate the restaurant with 30 days' notice, the Port and the traveling public are particularly vulnerable to business disruption due to the size and business volume of this particular restaurant. This is not the recommended alternative.

Alternative 2) – Execute one existing 5-year lease option. If the Port were to execute one of the existing five-year options, the lease would expire on June 30, 2020. This is beyond the necessary time needed to address the infrastructure issues of the opposite side of the Central Terminal. It also would delay the opportunity for the Port to determine if the marketplace might offer another type of concept and/or a more lucrative rent offer. This is not the recommended alternative.

Alternative 3) – Extend the current lease agreement through September 2017. This alternative will allow for continued operation of key restaurant capacity while there are construction impacts to food service in other portions of the Central Terminal. An extension also provides stability in employment at the restaurant for current employees. **<u>This is the recommended alternative.</u>**

ATTACHMENTS TO THIS REQUEST

- Exhibit A: PowerPoint Presentation
- Exhibit B: Draft Lease Amendment

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

- January 28, 2003 – Approval of Lease and Concession Agreement with Anton Airfoods to operate an Anthony's Restaurant in the Central Terminal.