PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
ACTION ITEM

Item No. 6c

Date of Meeting August 23, 2016

DATE: August 15, 2016

TO: Ted Fick, Chief Executive Officer

FROM: James Schone, Director, Aviation Business Development
Lionel Vincenti, Senior Manager, Airport Dining and Retail

SUBJECT: Airport Dining and Retail (ADR) Lease Group 3, Large Food Package 3 Addendum

Amount of This Request:	$-0-	**Source of Funds:**	NA
Est. Total Project Cost:	NA		
Est. State and Local Taxes:	NA	**Est. Jobs Created:**	195-250
Net Proceeds to the Port:	NA		

ACTION REQUESTED

Request Commission authorization to cancel Large Food Package 3 as part of the Airport Dining and Retail Program's Lease Group 3; to issue a new Large Food Package 4 in the same lease group and for the Chief Executive Officer to conduct competitive solicitations and execute lease and concession agreements with the selected proposers for this new Large Food Package 4.

SYNOPSIS

On June 14, 2016, the Port of Seattle Commission authorized the Chief Executive Officer to conduct competitive solicitations and execute lease and concession agreements with selected proposers for 12 new opportunities encompassing 24 units, collectively referred to as Airport Dining and Retail Lease Group 3 (LG3). The draft plan published in February 2016 for LG3 included three food and beverage units on the South Satellite (SS): SS-2A, SS-2B and SS-2C that are operated by Concessions International Inc. (CI) under a lease that expires on December 31, 2016. However, those units were removed from the final LG3 that was presented to and approved by the Commission. This was done due to the capital improvement plan existing at that point in time which had renovations to the SS starting within three years. Allowing the three SS units to be built as part of LG3 under that scenario would have led the Port to incur high costs associated with buying out the remaining net book value of the leasehold improvements made to those new units assuming 10 year leases.

During the past several months, additional planning has been done on the SS renovations project. The current expectation is that work will get underway at the earliest in four to five years. Thus, staff recommends the inclusion of the three SS units, currently under lease to CI, in a new lease package (Large Food Package 4) that will also include the four units currently in LG3/Large Food Package 3. This seven unit package will be competed via Request For Proposal process. The deadline for proposals to be submitted for this new lease package will be extended until November 2, 2016.

BACKGROUND

Leases for the majority of the Airport's dining, retail and personal service locations have expiration dates between mid-2015 and mid-2017. The large number of units with nearly simultaneous expiration dates is a consequence of the shift in management model that took place in the early part of the previous decade, specifically the move away from a master concessionaire model. The former master concessionaire operated nearly all of the Airport's dining, retail and duty free units from 1963 through 2004. In 2005, the Airport instituted a hybrid leasing structure of large prime operators of multiple units and direct leases with independent operators. Because nearly all leases after the master concessionaire were executed at the same time for similar lease term lengths, they have expiration dates very close to one another.

Port staff began working on an ADR Master Plan, the tool to plan and implement all the necessary steps to redevelop nearly 100 dining, retail and passenger service locations, in 2012. An important component of implementing this ADR Master Plan was that Commission would consider authorization for solicitation requests in groups of units and/or packages due to the large number of concurrent solicitation processes that would need to occur in order to efficiently move through the redevelopment process.

The Commission approved the first step of the redevelopment process in December 2014 with the approval of new leases and lease modifications with the ADR Program's largest lessees, HMS Host and Hudson Group. These leases are referred to as Lease Group 1 (LG1). In December 2015, Commission authorized the second step in the redevelopment effort: the issuance of competitive solicitations and execution of lease and concession agreements for 10 opportunities in Lease Group 2 (LG2) encompassing 13 units.

Continuing with the redevelopment process, ADR staff published a draft LG3 plan on the ADR leasing website in February 2016. This draft plan included a total of 14 opportunities encompassing 25 units. The purpose of publishing this draft LG3 plan was to make visible to current ADR tenants, potential ADR tenants and Port staff the expectations for units to be included in the next lease group so that additional due diligence could be completed before taking a final recommendation to Commission for authorization to proceed with competitive solicitations.

Two of the key issues that ADR staff were trying to address in the draft LG3 were the need for new dining investment in the SS as well as the looming expiration date (December 31, 2016) for the lease with CI. CI is a prime concessionaire at the Airport with five food and beverage units under a lease that was signed in 2004. Three of these units (Seattle's Best Coffee at SS-2A, Kobo at SS-2B and Runway Grill at SS-2C) on the SS share a common kitchen (see Exhibit A: South Satellite map), one unit (Seattle's Best Coffee at CD-3) is on D Concourse and one unit

(Seattle's Best Coffee at SE-2) is on the South Esplanade, pre-security. This lease also includes one sub-tenant, BF Foods, which operates a food and beverage unit on the North Satellite.

With those two key issues in mind, ADR staff included four units located on the South Satellite in the draft LG3/Large Food Package 3: SS-7 that is currently vacant as well as SS-2A, SS-2B and SS-2C that are the dining units operated by CI. The rationale for this package was to create opportunities for synergies and economies of scale for firms considering submitting proposals. This draft LG3 plan also proposed to submit the other two units operated by CI to competitive solicitations, but in different packages or units within LG3.

However, following publication of the draft LG3 plan, ADR staff learned that the early capital improvement plan for the SS renovations project forecast a construction start date in 2019, just three years from now. If these ADR units on the SS were built, and then the Port were to start the renovation work in 2019 as planned, the Port would potentially have to incur significant costs to buy out these ADR tenants of any unamortized value of their improvements in these units or have had to accept substantially lower rent proposals to offset the significantly reduced term. Based on that understanding, ADR staff made the decision to remove the three SS units (SS-2A, SS-2B and SS-2C) operated by CI and explore an extension to the CI lease for those units until such time as the SS renovation project got underway. That extension would have required additional capital investment by CI.

In June 2016, the Commission authorized the Port's Chief Executive Officer to conduct competitive solicitations and execute lease and concession agreements with selected proposers for the 12 new opportunities encompassing 24 units in LG3. The CD-3 and the SE-2 units operated by CI were included in the LG3 plan approved by Commission.

Following the ADR staff decision to remove the three SS units operated by CI from LG3, work continued on the development of the schedule for the SS renovations project. In early July, Port staff determined that due to significant construction in other parts of the Airport, construction of the SS renovations would likely not begin until four to five years from now at the earliest. With this new information, ADR staff now believes that it is in the best interest of all stakeholders to proceed with subjecting these units to competitive solicitations. Several options were explored to accomplish this as noted in the alternatives section of this memo.

The units (and associated concepts) currently included in LG3/Large Food Package 3 that were approved by Commission for competitive solicitations on June 14, 2016 (see Exhibit B) are:

- **SS-7: an upscale bar with food**.
- **CA-10: a marche (food hall) including a gourmet market and bar (minimum of wine and beer).** This location will be required to provide an area and related sound system to accommodate live music performances through the Airport's City of Music program.
- **CT-21: a quick service restaurant focused on Mediterranean or Asian food.**
- **CT-26**: **a sushi bar.**

The units (and associated concepts) to be included in the proposed LG3/Large Food Package 4 are:

- **SS-7: an upscale bar with food.**
- **CA-10: a marche (food hall) including a gourmet market and bar (minimum of wine and beer).** This location will be required to provide an area and related sound system to accommodate live music performances through the Airport's City of Music program.
- **CT-21: a quick service restaurant focused on Mediterranean or Asian food**.
- **CT-26: a sushi bar.**
- **SS-2A: a gourmet coffee unit**.
- **SS-2B: a quick service restaurant focused on Asian food.**
- **SS-2C: a national or local brand quick service restaurant serving hamburgers**.
- **South Satellite food court seating**: the successful respondent will be responsible for providing and maintaining seating for the three SS-2 units. The seat count must meet or exceed the current number of seats (206) in the seating area.
- **South Satellite Optional Food Service(s):** due to the limited space in the South Satellite, respondents will be encouraged to propose additional food service options for consideration by the Port. Such "Optional Food Service" items could include, but are not limited to: electronic ordering and holdroom food delivery (through applications or devices) as well as blended holdroom/dining concepts to further expand the food service offerings in the South Satellite.

Lease terms and the projected schedule for these units are contained in **Exhibit C**.

Authorization Approach

This proposed Lease Package 4 will be competed via the Request for Proposal (RFP) process with the same evaluation criteria and point allocation as approved by Commission on June 14, 2016.

SCHEDULE

The anticipated timeline for this new Lease Package 4 is outlined below**.** Upon execution of a lease agreement, the design review and permitting process can be anticipated to take up to six months followed by three to four months for construction before the commencement of business.

Projected Date	**Action**
August 23, 2016	Request for Commission authorization of Lease Group 3/Large Food Package 4
August 25, 2016	Issue addendum to LG3 and advertise the new Lease Food Package 4 via leasing website
Early September, 2016	Tours for interested businesses
August 25 through November 2, 2016	2 months for proposal preparation

November 2, 2016	Responses due
Late January, 2017	Port Evaluation Team completes their decisions
Early February, 2017	Notification to preferred respondents Update Commission on LG/Large Food Package 4 results
February and March, 2017	Lease Negotiations and Executions

STRATEGIES AND OBJECTIVES

The approval of this proposed change to LG3/Lease Package 4 supports the 25-year vision of the Port's Century Agenda to create 100,000 new jobs through economic growth led by the Port. These opportunities also support a number of the strategies and objectives of the Port's Century Agenda over the next quarter century:

- Advance this region as a leading tourism and business gateway;
- Promote small business growth and workforce development;
- Be the greenest and most energy efficient port in North America.

The Airport also has a number of shorter term strategic goals:

Strategic Goal:	Achieved Via:
Operate a world-class international airport	Meet the needs of tenants, passengers and the region's economy
Become one of the top 10 airports in customer service	Recruit quality operators that value staff training and development
Lead environmental innovation, minimize impacts	Lead sustainability programs to minimize waste and conserve water and energy
Reduce airline costs	Provide 50% revenue-sharing with airlines above specific debt service threshold
Maximize non-aeronautical income	Drive an increase in sales per enplanement to maximize growth in revenue
Develop valued community partnerships	Work in tandem with other Port resources, other partner agencies and community entities to foster partnerships

ALTERNATIVES AND IMPLICATIONS CONSIDERED

Alternative 1 - Combine the three CI units (SS-2A, SS-2B, and SS-2C) with one new unit (CD-1) for a new lease package of four units in LG3 with a potential opening in Q2 2018.
The CI lease for these SS units will be in holdover through Q4 2017.

<u>Economic implications:</u> As this alternative does not combine all the potential units on the South Satellite into one lease package, there will be less economies of scale potentially leading to lower bids.

Pros

(1) There would be no disruption to units in LG3 already approved by Commission.
(2) This allows for a faster opening of these three SS units compared to Alternative 2.
(3) The earlier build-out reduces the potential cost to the Port of buying out any unamortized improvements when the SS renovation project starts.

Cons

(1) The proposal deadline will need to be extended for this package.
(2) There creates an increased workload on Port resources i.e., the Project Management Group (PMG) and Airport Dining and Retail (ADR) staff.
(3) There is reduced time to re-concept the units and vet the financial feasibility of this package.
(4) This does not allow for potential synergies of combining three units in SS-2 with SS-7 as in Alternatives 4 or 5.

This is not the recommended alternative

Alternative 2 - Combine the three CI units (SS-2A, SS-2B, and SS-2C) on the SS with another unit (CD-1) to create a package of four units and compete via RFP in Lease Group 4 (LG4) with a potential opening in Q3 2018. This would require the CI lease to be holdover through Q1 2018.

Economic Implications: due to the delay in waiting until Commission authorizes competitive solicitations for LG4, likely in Q1 2017, there is potential for higher costs to the Port associated with buying out any unamortized improvements of these ADR units when the South Satellite renovation project gets underway.

Pros

(1) This allows more time to re-concept the units and vets the financial feasibility of this package.
(2) This increases the food elements in LG4 as currently, there is no large food package in that lease group.
(3) There would be no need to return to Commission until Q1 2017 when LG4 is presented for authorization.
(4) This creates more balance in LG4 between units competed via Competitive Evaluation Process vs. Request for Proposal Process.
(5) This does not create any delay in soliciting bids for units already included in LG3

Cons

(1) The delay in awarding leases and the associated opening date for SS units relative to Alternative 1 or 5 creates the potential for higher buy out costs when SS renovation project starts.
(2) The CI lease would need to be in holdover status longer than Alternative 1.
(3) This does not allow for the potential synergies of combining three units in SS-2 with SS-7 as in Alternative 5.

This is not the recommended alternative

Alternative 3 - Negotiate a new lease with CI for the three units on the South Satellite (SS-2A, B, and C) with the potential opening of these units in Q2 2017.

Economic Implications: As CI would be able to keep a portion of these units open while they complete the required upgrades to the units, this would have the least disruption to food service on the SS and thus, would have the least short-term impact on revenues.

Pros

(1) This has the least impact on level of service and short-term revenues as CI would be able to keep some portion of current units operating while they build out the new units.
(2) This has the least impact on PMG/ADR staff workload.
(3) This ensures service continuity for the workers currently employed by CI.

Cons

(1) This does not provide an equal opportunity for all firms to compete for these units.
(2) There is potential for new and better concepts if leases for these units are subjected to competition.
(3) Commission authorization would be required for a new lease with CI.

This is not the recommended alternative

Alternative 4 - Combine 3 CI units (SS-2A, B, and C) with one unit in LG3/Large Food Package 3 (SS-7) to create a four unit package and negotiate a new lease with another concessionaire with potential opening in Q2 2018. This would require replacing the SS-7 unit in LG3/Lease Package 3 with another unit in order to maintain a four unit package for purposes of competing via RFP. The CI lease would be in holdover until Q3 2017.

Economic Implications: As this alternative has the potential to create synergies and economies of scale for operators of the SS units, rent proposals could be higher.

Pros

(1) This creates an opportunity to increase seating capacity and improve the look and feel of the SS.

Cons

(1) There would be significant disruption to LG3.
(2) This does not provide an equal opportunity for all firms to compete for these units.
(3) There is potential for new and better concepts if leases for these units are subjected to competition.
(4) Commission authorization would be required for a new lease.
(5) In addition, Commission authorization must be received in order to solicit proposals for the revised LG3/Large Food Package #3.

This is not the recommended alternative

Alternative 5 - Combine the three CI units (SS-2A, SS-2B and SS-2C) on SS with four units (SS-7, CA-10, CT-21 and CT-26) already in LG3/Large Food Large Package #3 to create a new Large Food Package #4. This would form a seven unit package which would be competed via RFP with potential opening in Q2 2018. (See Exhibit C for all units proposed for this package). The CI lease for these SS units will be in holdover until Q4 2017.

Economic Implications: as this alternative leads to the earliest build-out of the units on the SS given a competitive solicitation process, the potential costs incurred by the Port to buy out any unamortized improvements of the ADR units when the SS renovation starts would be less. This alternative also creates the best potential for synergies and economies of scale for proposers, thus potentially leading to higher rent proposals.

Pros

(1) This creates potential synergies and economies of scale for future operators as LG3/Large Food Service Package #3 already includes the currently vacant SS-7 unit.
(2) In creating a seven unit package, there will be more economies of scale for proposers.
(3) This allows for an earlier opening of these three SS units.
(4) An earlier build-out likely reduces the potential cost of buying out any unamortized improvements when the SS renovation starts.

Cons

(1) The proposal deadline for this package will need to be extended.
(2) It increases the workload on Port resources (PMG and ADR staff).
(3) There is reduced time to re-concept and vet the financial feasibility of this package.
(4) The Central Terminal units in this new Large Food Package 4 may open after other Central Terminal quick service units that are also included in LG3.

This is the recommended alternative.

ATTACHMENTS TO THIS REQUEST

- Powerpoint presentation
- Exhibit A – South Satellite Map
- Exhibit B – Food Service Large 3
- Exhibit C – Food Service Large 4

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

- June 14, 2016 – Action) Request for Airport Dining and Retail Lease Group #3 Authorization
- May 24, 2016 – (Staff Briefing) – Briefing regarding proposed Airport Dining and Retail Lease Group #3.
- December 8, 2015 – (Action) Request for Airport Dining and Retail Group Lease Authorization

- November 24, 2015 - (Action) Request for Airport Dining and Retail Group Lease Authorization
- August 4, 2015 – (Action) Request for Airport Dining and Retail Group Lease Authorization
- February 24, 2015 – (Staff Briefing) Airport Dining and Retail Outreach and Leasing Plans
- December 9, 2014 – (Action) Authorization of Leases and Lease Modifications for HMS Host
- December 9, 2014 -- (Action) Authorization of Leases and Lease Modifications for Hudson Group
- December 9, 2014 – (Action) Amendment to Lease and Concession Agreement with Anton Airfoods (dba Anthony's Restaurant)
- November 25, 2014 – Commission Motion Regarding Job Quality
- September 30, 2014 – (Staff Briefing) Drivers for Phasing Decisions
- May 27, 2014 – (Staff Briefing) Airport Dining and Retail Master Plan
- September 11, 2012 – (Briefing) Airport Concessions Master Plan Update
- February 14, 2012 – Commission Motion Regarding Concessions Program Guidelines