**PORT OF SEATTLE**
**MEMORANDUM**

**COMMISSION AGENDA** | **Item No.** 5g
**Date of Meeting** December 6, 2011

**DATE:** November 22, 2011

**TO:** Tay Yoshitani, Chief Executive Officer

**FROM:** James R. Schone, Director, Aviation Business Development
Deanna Zachrisson, Manager, Concessions Business

**SUBJECT:** Lease and Concessions Agreement for Hudson Marketplace (former Borders Books)

## ACTION REQUESTED:

Authorization for the Chief Executive Officer to execute a lease and concession agreement with Airport Management Services, LLC, a Seattle Joint Venture (dba Hudson Group) to operate "Hudson Marketplace" in the Airport's Central Terminal for a term of seven (7) years.

## SYNOPSIS:

Staff requests approval of a 7-year lease and concession agreement with Airport Management Services, LLC dba Hudson Group to occupy a 3,432 square foot concessions location in the Central Terminal (CT-10, shown in Exhibit A). This location is the largest retail location in the Airport and is considered to be the 'anchor' tenant location for this part of the Airport. Borders Books vacated the unit on August 6, 2011 after a court-ordered liquidation of the company. The Hudson Group, an experienced airport-industry retailer, has provided a proposal to lease the space with favorable revenue terms for the Airport; a significant remodel investment by them; a long-term agreement; and vacating two other spaces that provide the Airport other future leasing opportunities. Efforts to lease the space to a local bookstore were not successful. The Hudson Marketplace will employ 18 new full-time employees.

## ADDITIONAL BACKGROUND:

The sales performance of Borders Books in the Central Terminal had been one of the best among the approximately 24 airport Borders locations nation-wide. The location generated $4 million in sales in 2010 and provided the Port with $464,000 in revenue. Because the location was left intact as a bookstore, staff initially sought to recruit a local bookstore to operate in the space. Two local bookstores submitted proposals and negotiations were initiated with one bookstore. However, these efforts did not result in a successful negotiation. A local bookstore in this location would likely have been able to sustain a similar level of sales as Borders; however, in the aviation concessions industry, there is a general lack of confidence in the medium-term future for bookstores. Although airport bookstores are presumed to fare better than street-side retail stores, electronic e-readers and smart phones have simply reduced the overall demand for printed material.

Airport staff was approached by Hudson Group with a proposal for a new concept in airport retail for the former Borders space. Hudson Group has a long history as an operator of airport stores and currently has a long-term contract for 22 news/gift and retail locations at the Airport. Its news/gift line of business also has felt the effects of the reduction in demand for printed material. Hudson proactively is seeking to identify and enter new market niches where strong customer demand exists. Their proposed concept is a new combination of 'grab and go' healthy foods, fruit, snacks and beverages, drugstore comparable 'over-the-counter' medicines, full-size personal care products, and locally branded retail merchandise, in combination with a 'Tech on the Go' selection of technology products and traditional printed magazines and newspapers. Books will continue to be sold in two other dedicated Hudson bookstores on Concourses A and C, as well as in Hudson news/gift locations throughout the Airport.

The Hudson Marketplace name reflects the breadth of the product assortment, including categories not currently served by any airport concessionaire. The addition of the 'grab and go' healthy food offering, with a lower price point than its closest competition, will add another alternative for travelers. Most Central Terminal retail and quick serve concepts have by 2010 achieved 100% or better of the sales anticipated to be achieved by 2015. Staff believes that Hudson Marketplace has the right offering to complement rather than disrupt the existing mix. It also represents another opportunity to appeal to the nearly 25% of airport travelers that make no purchases at the Airport.

The financial terms proposed are exceptional, particularly in comparison to the previous bookstore tenant. The proposed minimum annual guarantee (MAG) of $800,000 is roughly twice the MAG from Borders Books. Forecasted sales for the new concept are aggressive: $6.5 million in the first year, which compares to $4 million under Borders. Staff believes that the Hudson sales forecast is realistic based on the similar sales performance of other Hudson news/gift locations in the Airport.

Hudson Group currently operates four of seven retail units in the Central Terminal – three specialty retail and one news/gift kiosk. Due to this already high concentration in the Central Terminal, staff has negotiated with Hudson for the return of two key retail locations in or near the Central Terminal for re-leasing to new retail tenants in 2012. Adding new diversity to the Central Terminal retail core offers the opportunity for exciting new passenger amenities, as well as represents a new business opportunity for retailers. The specific locations are currently operated as a news/gift store and as Discover Puget Sound gift shop (CB-06 and CT-06, shown in Exhibit A). Staff anticipates working with the Airport's future leasing consultant to identify tenants for these locations. The Commission approved the procurement of concessions leasing consultant services in July 2011, and this procurement is anticipated to be complete by early 2012. Hudson will continue to operate both units until new tenants are ready to begin re-concepting the locations, anticipated for the fall of 2012.

Hudson Group will invest $1.2 million in the build-out of the new marketplace concept, with plans to open for business by May 1, 2012. In addition to this planned investment of approximately $350 per square foot, Hudson Group will return the two retail units to the Port with no claims of reimbursement for their remaining Net Book Value, equaling $798,000. The finishes and remaining fixtures in these units will be a benefit to the prospective new tenants.

## PROJECT JUSTIFICATION:

Approval of this lease will allow the Port to generate revenue from a vacated unit, and over the term of the lease earn significantly higher revenues than the previous bookstore concept.

Specific benefits of this agreement:

- Secures an exceptional financial commitment by Hudson Group.
- Commits a financially stable and experienced operator in a local ACDBE (Airport Concessions Disadvantaged Business Enterprise) joint venture partnership.
- Offers a unique marketplace concept which will generate high revenue in a large footprint, and become the anchor retail location for the Central Terminal.
- Proposed architectural plans allow for a more customer-flow friendly open corner at the confluence of Concourses A and B and Central Terminal.

## PROJECT STATEMENT AND OBJECTIVES:

***Project Statement:***
Open a new marketplace retail concept, Hudson Marketplace, in the Central Terminal unit known as CT-10 by May 1, 2011. The unit will be operated by Hudson as a bookstore and news/gift location on a temporary license until this time. Two current Hudson units will be re-let to new retail tenants later in 2012.

***Project Objectives:***
- Increase revenues to the Port.
- Offer the traveling public a new concept in mixed food/retail, drugstore, entertainment and technology products.
- Provide new employment opportunities.

## PROJECT SCOPE OF WORK AND SCHEDULE:

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|---|---|
| Execution of agreement | December 15, 2011 |
| Design approvals | January-February 2012 |
| Unit refurbishment | March-April 2012 |
| Open for business | May 1, 2012 |

## FINANCIAL IMPLICATIONS:

### Financial Summary:

| | |
|---|---|
| Concept: | Hudson Marketplace |
| Lease Term: | 7 years |
| Guaranteed MAG: | $800,000 |
| Percentage Rent: | 17% |
| Projected Sales Year One: | $6,500,000 |
| Estimated Port Revenue Year One: | $1,105,000 (MAG & percentage rent) |

## ECONOMIC IMPACTS AND BUSINESS PLAN OBJECTIVES:

This lease and concession agreement will contribute to achievement of the Airport's business plan objective of "maximizing non-aeronautical net operating income" by generating increased non-aeronautical revenues.

## BUSINESS PLAN OBJECTIVES:

The approval of this lease and concession agreement meets the Airport strategic goal of maximizing non-aeronautical net operating income consistent with current contracts, appropriate use of Airport properties and market demand. This proposal makes excellent use of Airport facility concessions spaces while also providing other benefits:

- Maximizes financial performance by meeting customer demand.
- Provides compelling customer and community value by bringing a new concept into a key retail location.
- Develops a new business opportunity for a stable operator with local ownership interest.
- Provides additional opportunities for new employees and suppliers to this business.

## ENVIRONMENTAL SUSTAINABILITY AND COMMUNITY BENEFITS:

- The proposed new tenant is committed to re-use as many fixtures left in the unit as possible. Fixtures that are not re-used for the new concept will be donated to Habitat for Humanity's retail outlet in Seattle. New materials will be durable and chosen for the airport environment, manufactured and/or used in an environmentally sensitive fashion.

- Hudson Marketplace will employ 18 new full-time employees.

## TRIPLE BOTTOM LINE:

The selection of the Hudson Marketplace as the new Central Terminal anchor concept supports a "triple bottom line" philosophy that values the concurrent pursuit of positive economic, social and environmental outcomes.

## ALTERNATIVES CONSIDERED AND THEIR IMPLICATIONS:

**1. Identify a new local bookstore tenant**
The two local bookstores, which initially were interested in leasing this location, were among the most stable in the Seattle area. While leasing to a local bookstore may be possible, the financial return to the Port would not be as favorable as the current proposal due to the uncertainty in the bookstore business. This is not the recommended alternative.

**2. Allow future leasing consultant to identify a new tenant**
The future leasing consultant is not anticipated to be under contract until early 2012, which would lead to delay of a permanent solution for the Borders vacancy. There also is no reason to anticipate that the future leasing consultant would be able to identify another type of tenant that can provide similar financial return to the Port. For example, specialty retail in this location instead of the proposed marketplace concept would not produce higher revenues due to lower gross sales and lower typical rent for specialty retail. This is not the recommended alternative.

**3. Approve the proposed lease and concession agreement**
The proposed agreement achieves the best possible financial return to the Port and provides future business opportunities for new retail operators in the locations that Hudson will be returning to the Port. **This is the recommended alternative.**

## OTHER DOCUMENTS ASSOCIATED WITH THIS REQUEST:

Exhibit A: Power Point Presentation
Exhibit B: Draft Lease and Concession Agreement

## PREVIOUS COMMISSION ACTIONS OR BRIEFINGS:

On August 9, 2011, the Commission authorized entering into a lease termination agreement for the former Borders bookstore location at Seattle-Tacoma International Airport, including the payment of $70,000 to the Borders Group, Inc., bankruptcy estate in consideration for the lease termination and release of the Airport lease from the bankruptcy liquidation proceedings.