**COMMISSION**
**AGENDA MEMORANDUM**

**Item No.** 9a

**Date of Meeting** March 8, 2022

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**TO:** Stephen P. Metruck, Executive Director

**FROM:** Dawn Hunter, Interim Aviation Chief Operating Officer
Khalia Moore, Senior Manager, Airport Dining and Retail

**SUBJECT: Adjustments to Airport Dining and Retail (ADR) Leases**

## ACTION REQUESTED

Request Commission authorization for the Executive Director to extend all ADR Multi-Premise Leases (as defined hereinbelow) and single use leases in Lease Groups 2, 3, 4, and 4a (Affected Tenants) by three (3) years, with the exception of Lease No. 2361 (as defined hereinbelow) and introductory and intermediate single use kiosk leases.

## EXECUTIVE SUMMARY

Certain Airport Dining and Retail (ADR) tenants were previously awarded leases at the Seattle-Tacoma International Airport (Airport) through a competitive process in lease groups referred to as two, three, and four (Affected Tenants). These Affected Tenants have alleged negative financial impacts resulting from expenses well beyond their anticipated bids giving rise to unforeseen build-out costs at the Airport. To address this challenge, on December 14, 2021, the Port Commission adopted an Order directing the Executive Director to evaluate the levels of financial impacts experienced by the Affected Tenants and recommend appropriate relief. The recommended approach is to extend the leases of Affected Tenants by 3 years.

## BACKGROUND

In response to concerns raised by Affected Tenants, the Port of Seattle (Port) completed a Tenant Build-Out Analysis (Build-Out Analysis) that examined the overall design and construction process for ADR tenants. Following the Build-Out Analysis, the Port developed recommendations for Airport ADR tenant buildouts that addressed these additional costs. These adopted recommendations include the following:

(1) Develop a new ADR plan with subject matter experts at the table including the tenants;

(2) Evaluate Port standards and to create ADR-specific standards that would be included in future request for proposals;

(3) Re-evaluate base building conditions based on new ADR plan;
(4) Prior to tenant design, Port will demolish the space and provide a "vanilla shell;"
(5) After demo, Port will verify as-built conditions with the new tenant;
(6) Port will address any necessary base building conditions;
(7) Port standards impacting ADR tenants will be discussed and approved with Aviation Commercial Management/ADR team prior to implementation to understand and analyze business and cost impacts to the tenants/program; and
(8) Subject matter experts shall be included during key planning decisions.

These recommendations were discussed with Aviation leadership and have now been adopted as best practices moving forward (Best Practices). As these Best Practices were implemented after Affected Tenants completed their respective buildouts, the Affected Tenants did not receive the benefit of them.

Certain Port leases included multiple premises under one tenant (Multi-Premise Lease(s)) in which the term for all the premises would run from the last to open premise under the lease. This resulted in all the premises under Multi-Premise Leases, except for the last to open, receiving longer lease terms than those under single premise leases. Thus, those tenants under the Multi-Premise Leases collectively received some additional time to amortize their tenant improvements and other startup costs. There is specifically one tenant under a Multi-Premise Lease that is distinguishable from all other tenants (that certain *Lease and Concession Agreement for Food and Beverage Operations, between the Port of Seattle and Host LPI SEA FB, LLC, dated May 16, 2018, as amended* and referred herein as "Lease No. 2361"), because its term was extended for a period of ten (10) years, seven (7) months between the opening of the first premise under the lease and the last to open. There are also introductory and intermediate single use kiosk leases; however, the initial investment associated with these leases is not considered as substantial and is distinguishable from the other tenants in these lease groups.

## JUSTIFICATION

Port staff reviewed the actual build out cost compared to that of the original anticipated bid of a representative tenant of each type of use from the Affected Tenants (retail, restaurant, and service). Staff then compared the difference between the expected buildout cost and the overrun of those costs to the anticipated timeframe for the return on investment. The results of this comparison resulted in a determination that it would take these representative tenants an average of three (3) years to make up the losses associated with the extra buildout costs. As such the recommended alternative is to extend the leases of the Affected Tenants by three (3) years to set off these losses. Staff has suggested to exclude Lease No. 2361 as this tenant has benefited by receiving a collective extended term through its lease structure.

## ALTERNATIVES AND IMPLICATIONS CONSIDERED

Several factors were considered when deliberating upon alternatives, including financial impacts, impacts to personnel, equity, and FAA requirements. The recommended alternative meets standards related to avoiding exclusive uses and impacts on ACDBE tenants. The Airport has no exclusive use ADR leases, offers a variety of uses, and the Airport will be extending new ADR opportunities that will be released for competitive bid during the Affected Tenant lease terms. The current variety of uses within the Airport include many restaurants (i.e., sit-down, fast food and counter service), retail (i.e., a variety of products from convenience, clothing, art, luggage, electronics, etc.), and services (i.e., spa, shoeshine, and currency exchange). The majority of ADR tenants being granted extensions through this proposal include ACDBE participation and represent a variety of uses. In addition, Port staff will meet with the ACDBE tenants prior to implementing the proposed extensions to ensure these extensions do not negatively impact them.

**Alternative 1** –In lieu of lease extensions, provide Affected Tenants with an equitable monetary payment to address the additional cost.

<u>Cost Implications</u>: Unknown but could equate to several million dollars.

<u>Pros</u>: No lease extensions would be necessary or warranted.

<u>Cons</u>: This could result in a significant financial impact to the Port and to public funds. Furthermore, it would require a tremendous amount of personnel resources and time to carry out the required calculations.

This is not the recommended alternative.

**Alternative 2** – Provide lease extensions to all Multi-Premise Leases (other than Lease No. 2361) and single use leases (excluding introductory and intermediate kiosk leases) by five (5) years.

<u>Cost Implications</u>: No monetary cost to the Port. The Port will financially benefit from the longer lease term in significant costs savings of replacing these tenants, such as procurement and build-out costs for new ADR tenants.

<u>Pros:</u> Tenants would have a longer term in which to amortize their investments while sustaining revenue being generated at the Airport.

<u>Cons:</u> The longer extension hinders newer concepts from coming into the Airport and is not justified according to the Port's analysis.

This is not the recommended alternative.

**Alternative 3** – Provide lease extensions to all Multi-Premise Leases (other than Lease No. 2361,) and single use leases (excluding introductory and intermediate kiosk leases) by three (3) years.

Cost Implications: No monetary cost to the Port. The Port will financially benefit from the longer lease term in significant costs savings of replacing these tenants, such as procurement and build-out costs for new ADR tenants.

Pros: Tenants will be granted additional term in which to amortize their investments at a term which is equitable in light of the additional unforeseen costs associated with their build-out. Revenue continues to be generated at the Airport with no out of pocket expense to the Port.

Cons: The extension delays newer concepts from coming into the Airport.

***This is the recommended alternative.***

## FINANCIAL IMPLICATIONS

The are no negative monetary impacts associated with recommended alternative. The Airport shall continue to receive revenue and will benefit as there will be no interruption of revenue for a change in tenant/concept and the Port will postpone the associated procurement and build-out costs for an additional three (3) years.

## ATTACHMENTS TO THIS BRIEFING

(1) Presentation

## PREVIOUS COMMISSION ACTIONS OR BRIEFINGS

December 14, 2021 – Commission approved a Motion directing the Executive Director to evaluate the levels of financial impacts experienced by Airport Dining and Retail Tenants and recommend appropriate relief.