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CITY OF LONG BEACH

DEPARTMENT OF ECONOMIC AND PROPERTY DEVELOPMENT
333 West Ocean Boulevard 3RD Floor • Long Beach, CA 90802 • (562) 570-6099 • Fax (562) 570-6380

November 1, 2016

HONORABLE MAYOR AND CITY COUNCIL
City of Long Beach
California

RECOMMENDATION:

Authorize the City Manager, or designee, to execute any and all documents, including additional lease and capital funding provisions, necessary for an Amended and Restated Lease and Operations Agreement No. 22697 with Urban Commons, LLC, for the Queen Mary and adjacent properties; and,

Authorize the City Manager to proceed with funding up to $23 million in infrastructure repairs to the Queen Mary by using up to $5.8 million in total reserves designated for the Queen Mary and borrowing approximately $17.2 million to be repaid from Queen Mary related revenues. (District 2)

DISCUSSION

On November 17, 2015, the City Council authorized the City Manager to execute an Amended and Restated Lease and Operations Agreement No. 22697 (2015 Amended and Restated Lease) with Urban Commons, LLC (Urban Commons), as Successor Lessee to Garrison Investment Group, LLC (attached). The previous action also authorized the assignment of the 2015 Amended and Restated Lease from Garrison Investment Group, LLC to Urban Commons, LLC. Significant deal points of the 2015 Amended and Restated Lease included making capital improvements to the Queen Mary using City revenue from Carnival Corporation (Carnival) passenger fees. Another key deal point was the requirement for Urban Commons to sublease the entire dome to Carnival for expanded terminal operations to accommodate larger cruise ships, the first of which is expected to arrive in January 2018. The other major deal point was to ensure that Urban Commons had the financial capability to develop the land surrounding the Queen Mary.

Subsequent to the approval of the terms by the City Council on November 17, 2015, the negotiations between Urban Commons and Carnival to accomplish several of the deal points were more complicated, and more costly to implement than initially anticipated; therefore, the 2015 Amended and Restated Lease was not executed.

The City and Urban Commons have now agreed to changes in lease terms associated with urgent Queen Mary repairs and the replacement passenger facility. The proposed changes to the lease terms (2016 Amended and Restated Lease) and the impacts to the City are outlined as follows:

Urgent Queen Mary Repairs

The 2015 Amended and Restated Lease provided that Urban Commons would continue to assume responsibility for maintenance and repair of the Queen Mary. However, due to the age and location of the ship, there are significant structural and utility deficiencies requiring urgent attention. In order to protect this City asset, the 2015 Amended and Restated Lease contemplated that the City would participate by annually pledging revenues to be used for capital projects and historic preservation. These revenues would be deposited into a reserve account, called the Historic Preservation Capital Improvement Plan (HPCIP) fund.

HPCIP funding would come from Passenger Fee Revenues paid annually by Carnival to Urban Commons and passed-through to the City (estimated at $2.15 million) and Base Rent paid annually by Urban Commons ($300,000). The level of urgently needed repairs requires an investment in excess of this annual revenue stream. Therefore, City staff and Urban Commons have negotiated a plan in which the City would provide significant upfront funds for capital repairs and renovations to the Queen Mary. The proposal uses existing cash reserves currently designated for the Queen Mary (up to $5.8 million) and a ten-year City bond issue of about $17.2 million to provide up to $23 million for repairs agreed upon by the City and Urban Commons. Payment of the debt service on the bond issue will come from future Passenger Fee Revenues and Base Rent during the first seven years of the 2016 Amended and Restated Lease. These revenues would have been deposited in the HPCIP fund for preservation, conservation, and restoration of historical assets associated the Queen Mary, but will instead, for the first seven years, be used to pay debt service on the bond issue to partially fund the needed immediate improvements. In addition, Urban Commons will divert a portion of its share of Passenger Fee Revenues in Years 6 to10.

The total repair needs of the Queen Mary far exceed the amount that will be funded by the proposed upfront funding, but the upfront funding will allow the highest priority repairs to be made in a timely manner and prevents further deterioration of the Queen Mary, and allow the revitalization and development of the associated property to move forward.

The revised lease terms related to the capital repairs of the Queen Mary are as follows:

2015 Amended and Restated Lease	2016 Amended and Restated Lease
Passenger Fee Revenues paid to the City will be deposited into an HPCIP fund annually to be used for preservation, conservation and restoration associated with historic aspects of the Queen Mary, and maintenance, repair and replacement of specific elements associated with the maritime nature of the ship.	No change.
Amount of HPCIP available to Urban Commons is limited to annual Passenger Fee Revenues and Base Rent paid by Carnival.	Within six months from signing the 2016 Amended and Restated Lease, the City will provide upfront funds of up to $23 million for capital repairs to the Queen Mary.
	City's revenue from Passenger Fee Revenues and Base Rent in Years 1-7 will be used toward repayment of City upfront funding or financing; Urban Commons' revenue from Passenger Fee Revenues in Years 6-10 will be used toward repayment of City's upfront funding or financing.

Deposits of Passenger Fee Revenues from Carnival into the HPCIP that would have been made annually will be directed toward repayment of financing in the first ten years of the 2016 Amended and Restated Lease; therefore, HPCIP funds will not be available to Urban Commons in the event of capital repair needs. However, this does not relieve Urban Commons from its responsibility for preservation, conservation, restoration, maintenance and repair of the Queen Mary.

Replacement Passenger Facility

During negotiations with Urban Commons, it became apparent that the use of the dome is integral to Urban Commons' long-term redevelopment plans as an event venue. This necessitated additional negotiation between Urban Commons and Carnival related to the construction of a new replacement passenger facility , which when completed, would make the dome available to Urban Commons. Urban Commons and Carnival have signed a Second Amendment to the Sublease, which details Urban Commons' responsibility to provide a replacement passenger facility to Carnival. The City and Urban Commons have agreed to amend the Revenue Sharing provision of the 2016 Amended and Restated Lease to increase the Passenger Fee Revenues paid to Urban Commons. The additional revenue to Urban Commons will defray the additional cost of construction of the replacement passenger facility and preserve capital for the commercial development of the land.

2015 Amended and Restated Lease	2016 Amended and Restated Lease
Years 1-5, Urban Commons will pay to the City all Passenger Fee Revenue Fee from Carnival, up to a maximum of $2.15 million per year.	No change.
Beginning on Year 6, Urban Commons will pay to the City all Passenger Fee Revenues from Carnival, up to approximately $2.15 million per year; thereafter, the parties will share excess Passenger Fee Revenues equally.	Years 6-15, Passenger Fee Revenues will be split equally, subject to the City receiving a minimum of $1.5 million per year. Beginning on Year 16, Passenger Fee Revenues will be split equally; subject to the City receiving a minimum of $2.15 million per year, adjusted from Year 1-16 based on the CPI, with an annual CPI thereafter of not more than 3 percent per year.

The reduction in revenue to the City is estimated at $5.375 million in the first ten years of the 2016 Amended and Restated Lease, which is the length of the bond issue. This will result in lower revenues than otherwise would have been deposited into the HPCIP fund.

City Bond Issuance

The City will provide up to $23 million for immediate repairs to the Queen Mary through a combination of Tidelands cash (up to $5.8 million previously designated for the Queen Mary) and a bond issue secured by a general pledge of Tidelands revenues, but intended to be repaid entirely by revenue received by the City and Urban Commons as previously described.

The bond issue is expected to be sized at approximately $19 million to provide about $17.2 million in construction proceeds. The bond issue would be backed by a pledge of all Tidelands revenue, including oil revenues and the transfer from the Harbor Revenue Fund. This is the same revenue backing used for the Aquarium Bond issue and the same as any future Tidelands debt. This bond issue thus weakens slightly the City's ability to borrow from Tidelands revenues in the future. The actual source of debt service payment is anticipated to be the Passenger Fee Revenues and Base Rent received from Urban Commons, as shown below.

Source of Revenue	Expected Revenue
City Passenger/Base Rent Revenue Years 1-5	$2.45 million per year for 5 years
City Passenger/Base Rent Revenue Years 6-7	$1.933 million per year (estimated) for 2 years
Urban Commons Passenger Fee Revenues Years 6-10 (50 percent of its 50 percent share)	$816,668 per year (estimated) for 5 years

The bond issue, to be repaid by the Passenger Fee Revenues and Base Rent revenue, has some risk to the City with regard to the sufficiency of the identified funding sources to pay debt service. The Economic and Property Development Department has reviewed the risk and concludes that the risk is low. Carnival is the largest vacation cruise line company in the world and owns other brands, including Princess, Holland America and Cunard. The City terminal is the only terminal owned by Carnival in the United States, which is very strategic to its operations (it is able to control vessel deployment, passenger handling, and terminal operations rather than paying a third party operator). The Southern California market for cruises is consistently strong. The Department believes that the strength of Carnival's business in the City outweighs the risk that Carnival will stop bringing vessels to Long Beach or that its business will deteriorate.

This matter was reviewed by Deputy City Attorney Richard F. Anthony on October 17, 2016 and by Budget Analysis Officer Julissa Josè-Murray on October 18, 2016.

TIMING CONSIDERATIONS

Upon the City Council's approval of the additional terms, the parties are prepared to sign the Amended and Restated Lease.

FISCAL IMPACT

To address urgent repair needs at the Queen Mary, the City will provide up to $23 million through the use of Queen Mary reserves of up to $5.8 million and a bond issue netting approximately $17.2 million in construction proceeds as outlined above. There is a minute risk that market changes may preclude the City from issuing the expected debt in a timely manner. The Financial Management Department believes this to be extremely unlikely. However, if the financing is delayed, the City will temporarily redirect money from existing resources and reserves and replenish that money as soon as debt can be issued.

Additionally, to facilitate private development of the replacement passenger facility for Carnival by Urban Commons, the per Passenger Fee Revenue distribution methodology in the lease agreement will be revised. The proposed methodology will redirect approximately $1 million annually of per Passenger Fee sharing revenues from the City to Urban Commons during Years 6-15. In the unlikely event that the replacement passenger facility is never constructed by Urban Commons, then Urban Commons, at its expense, will be required to construct an alternate facility (subject to City's reasonable approval) intended to provide a general benefit to the public.

The Passenger Fee Revenues being redirected from the HPCIP fund for debt service or the new passenger facility, will not be available for Queen Mary preservation, conservation, restoration, maintenance and repair during that time, although the monies being redirected to pay debt service will be used to fund immediate, instead of future, repairs. Beginning in Year 16 the HPCIP is anticipated to resume receipt of its projected annual funding at $2,450,000.

SUGGESTED ACTION:

Approve recommendation.

Respectfully submitted,

KATHRYN MCDERMOTT
INTERIM DIRECTOR OF
ECONOMIC AND PROPERTY DEVELOPMENT

Attachment

APPROVED:

PATRICK H. WEST
CITY MANAGER

CITY OF LONG BEACH

R-14

DEPARTMENT OF ECONOMIC AND PROPERTY DEVELOPMENT
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November 17, 2015

HONORABLE MAYOR AND CITY COUNCIL
City of Long Beach
California

RECOMMENDATION:

Authorize the City Manager, or designee, to execute any and all documents necessary for an Amended and Restated Lease and Operations Agreement No. 22697 and concurrent assignment to Urban Commons, LLC, as Successor Lessee to Garrison Investment Group, LLC. (District 2)

DISCUSSION

The Queen Mary is a City-owned asset operated under Lease and Operations Agreement No. 22697 (Lease) with Save the Queen, LLC (STQ). In late 2007, STQ assumed control over Queen's Seaport Development, Inc., and the Lease through bankruptcy proceedings of the ship's prior operator. Subsequently, Garrison Investment Group, LLC (Garrison) foreclosed on STQ and assumed ownership and control of the Leasehold interest. Since that time, Garrison has been an excellent steward of the Queen Mary. Garrison has spent over $13 million dollars on preservation and renovation, and exceeded capital improvement requirements established during bankruptcy proceedings. Additionally, Garrison and their management company, Evolution Hospitality, have modernized opertions, improved retail and restaurant offerings, and brought new and exciting events and exhibits to the ship.

Garrison has done a tremendous job of managing the Queen Mary hotel, attractions and events; however, as an investor, they did not intend to operate the Queen Mary in the long-run or develop the adjacent shoreside property. Consequently, Garrison has conducted an exhaustive search to identify a successor lessee (Successor Lessee) who will maintain excellent stewardship; continue to preserve, restore and maintain the ship; and demonstrate sufficient capitalization and experience to promptly proceed with shore-side development. Urban Commons, LLC, (Urban Commons) was selected by Garrison as their preferred Successor Lessee. Urban Commons is a Los Angeles based real estate investment and development firm specializing in innovative hospitality and entertainment destination developments. Urban Commons has development experience, not only in the Los Angeles area, but also in the Bay Area, Silicon Valley, Central Coast, Pasadena, Palm Desert, and Miami.

City staff have spent considerable time reviewing the financial stability of Urban Commons, their familiarity with the constrains of site development, and their ability to manage an extensive outreach, entitlement and development process. Urban Commons has demonstrated the necessary experience and financial capacity to operate a combined historic hotel and event/attraction facility, and the ability to undertake new development on the unimproved portions of the leasehold area.

The challenging structure of the existing lease has served to be an impediment to investment into preservation, restoration and shore side development. As a result, City staff, Garrison and Urban Commons propose a number of modifications that serve to address these issues. City staff have worked diligently to craft an agreement that would promote shore side development, while also strengthening the capital and preservation support for the Queen Mary. To this end, City staff have negotiated the proposed Amended and Restated Lease No. 22697 containing the following major terms and provisions:

- **Lessor:** City of Long Beach

- **Current Lessee:** Save the Queen, LLC, a wholly owned subsidiary of Garrison Investment Group, LLC

- **Successor Lessee:** Urban Commons, LLC

- **Leased Premises:** 64.22 Acres (43.38 acres land area/20.84 acres water area)

- **Lease Term:** 66 years from execution of Amended and Restated Lease.

- **Minimum Rent:** $300,000 annually, payable monthly in advance. CPI adjustment on each 10-year anniversary of commencement date, not to exceed 40% in any 10-year period. This reflects an annualized increase of approximately 3.4%.

- **Priority Return:** Priority Return on initial Stipulated Investment Basis (purchase price for the leasehold interest) and eligible capital investments, to the extent it is available from Operating Revenue, shall be paid to the Successor Lessee on an annual basis at a rate of 9%. Priority Return shall not be cumulative.

- **Percentage Rent:** Percentage Rent will be calculated at 10% of Operating Revenue after Successor Lessee achieves its Priority Return, and payable to the extent it exceeds annual Minimum Rent.

- **Land Rent:** The Amended Lease will provide flexibility for the Successor Lessee to terminate the Amended Lease as to individual development parcels, subject to receipt of applicable entitlements, and for Successor Lessee (or its assignee) to enter into new, financeable ground leases for development purposes, not to exceed the term of the underlying 66-year lease.

  Land rent shall be based on appraised value to be established at the time of execution of the Amended Lease, with payments beginning when the land included in financeable ground leases generates revenue, either directly or indirectly. Land values shall increase by CPI adjustment on each 10-year anniversary of commencement date, not to exceed 40% in any 10-year period.

- **Participation in Sales and Refinance:** The City shall be entitled to participate in any net profits from either the sale or refinance of the entire leasehold generally at the level of 25% of net proceeds after transaction costs and Successor Lessee's required return.

- **Base Maintenance and Replacement Plan:** Successor Lessee shall be required to establish a new Base Maintenance and Replacement Plan (BMRP) fund. Successor Lessee shall set aside a percentage of Gross Revenues, to fund the capital investment required for continued first class operation of the hotel, event and atttraction facilities as follows: 1% during the first and second years; 2% during the third and fourth years; and 3% each year thereafter.

- **Historic Preservation and Capital Investment Plan:** Successor Lessee shall prepare a Historic Preservation and Capital Investment Plan (HPCIP) for preservation, conservation and restoration associated with the special historic status of the ship; and maintenance, repair or replacement of specific elements associated with the maritime nature of the ship.

  Funding for the HPCIP will be provided by all or a portion of revenues received from Carnival Passenger Fees; all or a portion of the Minimum Rent paid to the City (excluding the Catalina Express pass-through rent and rent from special events); and any grant funds or other special source funds the City is able to obtain for this purpose. Successor Lessee may contribute additional funds needed to complete the projects on the approved HPCIP, which shall be eligible capital investments and added to the Stipulated Investment Basis for the purpose of calculating Preferred Return.

- **Compliance with Applicable Laws:** Successor Lessee shall comply with all requirements that may be reasonably imposed on the Queen Mary to comply with laws, including compliance with the Americans with Disabilities Act (ADA). These improvements will be considered as eligible capital investments and added to the Stipulated Investment Basis for the purpose of calculating Preferred Return.

- **Financial Reporting:** Financial reporting practices are to be modified to conform to the changes recommended in the City Auditor's Report of September 12, 2012 (including flow of all revenue to a single entity and associated auditing requirements, financial reporting and formatting requirements, etc.).

- **Queen Mary Heritage Foundation:** The Current Lessee has assisted in the establishment of the non-profit Queen Mary Heritage Foundation (QMHF), whose mission and purpose is to support historic preservation, conservation and restoration improvements pertaining to the ship, its historic artifacts and ephemera, and to serve as a vehicle to educate and disseminate information concerning the ship's history. Successor Lessee shall support and participate on the governing board of the Queen Mary Heritage Foundation (QMHF), and the City shall have ex-officio representation on the governing board.

Any and all funds raised by the Foundation and used in support of improvements to the ship shall be not added to the Stipulated Investment Basis for the purposes of calculating Priority Return, and said funds shall be subject to financial reporting requirements and auditing by the City.

- **Restructuring of Carnival Dome Lease:** At a time of mutual agreement between Successor Lessee and Carnival Corporation (Carnival), Successor Lessee shall sub-lease the entire Carnival Dome to Carnival for expanded terminal operations. Each year of the first five years of the Amended Lease term, Successor Lessee shall pay to City an amount equal to the passenger fees received by Successor Lessee from Carnival for the prior year up to a maximum of $2,150,000 (the "Base Dome Payment"). City shall deposit the Base Dome Payment into an account to which both City and Successor Lessee have mutual access (the "HPCIP Account") for the purpose of capital projects and historic restoration. During the first five years of the Amended Lease term, all passenger fees received by Successor Lessee from Carnival in excess of the Base Dome Payment shall be retained by Successor Lessee. City shall have the right to collect passenger fees directly from Carnival if and to the extent Successor Lessee fails to make the Base Dome Payment.

  Beginning in the sixth year of the Amended Lease term and each year thereafter, Successor Lessee shall pay to City all passenger fees received by Successor Lessee from Carnival up to $2.15 per passenger. Successor Lessee shall further pay to the City 50% of passenger fees generated in excess of $2.15 per passenger. The other 50% shall be retained by the Successor Lessee and included as revenue for financial reporting purposes. City revenue derived from passenger fees shall be deposited into the HPCIP Account and may be used only to fund HPCIPs as provided above.

The proposed Amended and Restated Lease No. 22697 will faciliate and encourage innovative shore side development, and provide a secure funding source for the historic preservation of, and capital investment into the Queen Mary. Additionally, the Current Lessee and Successor Lessee have expressed keen interest in working coopertaively with the Queen Mary Task Force in connection with outreach, entitlement and development of the leasehold area.

This matter was reviewed by City Attorney Charles Parkin on November 5, 2015 and by Assistant Finance Director Lea Eriksen on November 4, 2015.

TIMING CONSIDERATIONS

City Council action on this matter is requested on November 17, 2015 in order to ensure that the Amended Lease can be executed before the end of the year.

FISCAL IMPACT

Annual rent revenue of approximately $300,000 will be redirected from the Tidelands Operating Fund (TF 401), which is currently used to support general Tidelands Operations, to the Queen Mary Fund (TF 410) in the Department of Public Works (PW), where it is restricted for capital expenses and investments for the Queen Mary. These funds and the Carnival Passenger Fees will be available to fund the Historic Preservation and Capital Investment Plan for the Queen Mary and will be managed by the Department of Economic and Property Development. Approval of this recommendation will provide continued support to the local economy.

SUGGESTED ACTION:

Approve recommendation.

Respectfully submitted,

MICHAEL P. CONWAY
DIRECTOR OF ECONOMIC &
PROPERTY DEVELOPMENT

MPC:JMV

APPROVED:

PATRICK H. WEST
CITY MANAGER