

CITY OF LONG BEACH

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 operations, 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 constraints 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 attraction 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 facilitate 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 cooperatively 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.

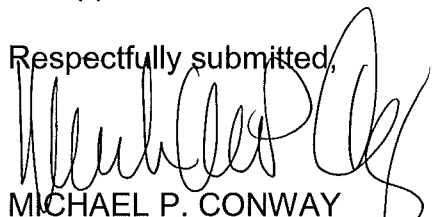
FISCAL IMPACT

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