AGENDA REPORT

Ordinance: Approval and Authorization for Execution of an *Amendment to Lease* with DHL Express (USA), Inc. at the North Field of Oakland International Airport, to Extend its Occupancy of a Warehouse, Land and Apron for Five (5) Additional Years at an Initial Rental of $43,848 Per Month. **(Aviation)**

MEETING DATE:	11/30/2017
AMOUNT:	$43,848 Monthly Rental – Revenue
PARTIES INVOLVED:	DHL Express (USA), Inc. Michael J. Copland, Senior Manager Corporate Real Estate and Airport Affairs
SUBMITTED BY:	Bryant L. Francis C.M., Director of Aviation
APPROVED BY:	J. Christopher Lytle, Executive Director
ACTION TYPE:	Ordinance

EXECUTIVE SUMMARY

This action would give first reading to an ordinance to (i) approve the terms and conditions of an *Amendment to Lease* with DHL Express (USA), Inc. to extend for five (5) years its occupancy of a warehouse, paved and unpaved land, and apron at the North Field of Oakland International Airport for a monthly rent of $43,848; and (ii) authorize execution of the *Amendment to Lease* by the Executive Director.

BACKGROUND

DHL Express (USA), Inc. (“DHL”) has been a tenant at Oakland International Airport (“OAK”) since 1992, originally occupying a portion of Hangar 9 before relocating to the current premises in January 2008. DHL has previously operated one or two daily Boeing 767 Freighters as part of its Oakland-based domestic express package delivery business.

As illustrated in the aerial of OAK’s North Field, DHL now occupies a 1940s era warehouse building of approximately 40,000± square feet; 37,897± square feet of paved and partially-paved land; and, 115,859± square feet of apron used for both aircraft and vehicle parking. In exchange for the Port providing a ten (10) year term which expires on December 31, 2017, DHL invested more than $1.5 million in capital improvements to the premises, including developing modern office space within the warehouse, upgrading restrooms, modifying truck dock doors, improving infrastructure and energy efficiency, and constructing a 70' × 200' "annex" to the warehouse for its proprietary package conveyance and sorting equipment.

In early January 2009, shortly after completing its rehabilitation and expansion of the leasehold facilities, DHL made the strategic decision to end its domestic express delivery business throughout the United States so that it could focus exclusively on its international operations. DHL mothballed it leasehold facilities and its aircraft service at OAK ceased. DHL continued to pay its contractually obligated monthly rental while it searched for a subtenant, with Port staff assistance, but none was ever found.

In mid-2013, DHL reactivated the OAK facility as one of three Bay Area service centers. International packages arrive at San Francisco International Airport via five daily scheduled aircraft and then are delivered in large trucks/trailers to the service centers located in downtown San Francisco, Fremont and OAK, where the packages are further sorted and driven by courier van to final destinations. DHL has not restarted flight operations at OAK.

DHL has requested an extension of its *Lease* for up to an additional ten (10) years to continue operating the facility as its Oakland-area service center; Aviation staff recommends the transaction outlined in the Analysis section.

ANALYSIS

The market for air cargo facilities are limited, and if DHL were to vacate its leasehold upon expiration of the *Lease* at the end of Calendar Year 2017, the Port would have difficulty finding a new tenant for the space. Since DHL has not operated aircraft at OAK for almost nine years, but has paid significant rent for the apron (almost $18,000 per month attributable to aircraft parking areas), DHL has requested that the aircraft apron be removed from the premises. Staff believes this is a reasonable request because the aircraft apron can be used occasionally for itinerant aircraft parking. In exchange, DHL must remove the "annex" structure and repair any damage to the apron at its sole cost.

The Summary of Terms (Attachment "A") highlights the changes to be made between the existing *Lease* and the proposed *Amendment to Lease*; significantly:

- Five year extension term;
- Option to extend for five additional years if mutually agreed by the Port and DHL;
- Apron area to be reduced from 115,859 square feet to 17,560 square feet;
- Warehouse monthly rental rate to increase from $0.587 PSF to $0.599 PSF;
- Apron monthly rental rate to increase from $0.196 PSF to $0.290 PSF;
- Net monthly rental to decrease from $61,062 to $43,848 (attributable to the deletion of the aircraft apron area);
- Rental rates to adjust by CPI every 30 months (no change from *Lease*);
- Security Deposit set at $88,000 (approximately 2× monthly billings);
- DHL to assume maintenance for roof, skylights and exterior walls, in addition to the windows, doors and glass already included in the *Lease* (i.e., to be a NNN lease);
- DHL to demolish the annex and repair the underlying apron within the first six months of the extension term (subject to separate permit and Board action); and
- Employment provisions to be updated to reflect current Port policies.

The rental rates to be included in the *Amendment to Lease* are reflective of fair market rental value as determined by recently completed appraisals of similar properties located within close proximity to the leasehold at the North Field.

Not moving forward with approval of the *Amendment to Lease* to extend the term and make other adjustments would result in the *Lease* expiring and continuing on a month-to-month basis, and DHL then vacating the premises within a year. As noted above, DHL and the Port had difficulties finding an interested subtenant for the facilities in the past; therefore, it is likely the facilities would remain vacant with a corresponding loss of $43,848 in monthly revenue after DHL vacates sometime in 2018.

BUDGET & STAFFING

Staff has been negotiating the *Amendment to Lease* for several months and anticipated a net reduction in monthly rental. The adopted FY2017-18 Operating Budget assumed rental of $39,059 per month effective January 1, 2018 vs. the negotiated rental of $43,848 per month. For the balance of the FY18, there would be a positive variance of $4,788 per month or $28,734 for the next six months.

Approving the *Amendment to Lease* will not have any staffing impact.

MARITIME AVIATION PROJECT LABOR AGREEMENT (MAPLA)

The matters included in this Agenda Report do not fall within the scope of the Port of Oakland Maritime and Aviation Project Labor Agreement (MAPLA) and the provisions of the MAPLA do not apply.

STRATEGIC PLAN

The action described herein would help the Port achieve the following goals and objectives in the Port's Strategic Plan

(http://www.portofoakland.com/pdf/about/strategicPlan2011-2015.pdf)

Goal A: Create Sustainable Economic Growth for the Port and Beyond

- Goal A: Objective 1: Maximize the use of existing assets.

Goal B: Maintain and Aggressively Grow Core Businesses

- Goal B: Objective 1: Retain existing customers and tenants.

LIVING WAGE

Living wage requirements, in accordance with the Port's Rules and Regulations for the Implementation and Enforcement of the Port of Oakland Living Wage Requirements (the "Living Wage Regulations"), apply to this agreement as the tenant employs 21 or more employees working on Port-related work and the tenancy agreement is greater than $50,000.

ENVIRONMENTAL

The proposed agreement is categorically exempt from the requirements of the California Environmental Quality Act (CEQA) pursuant to Section 15301 Existing Facilities, which exempts the operation, repair, maintenance, permitting, leasing, licensing, or minor alteration of existing public or private structures, facilities, mechanical equipment or topographical features, involving negligible or no expansion of use beyond that existing at the time of the lead agency's determination.

GENERAL PLAN

This action does not change the use of any existing facility, make alterations to an existing facility, or create a new facility; therefore, a General Plan conformity determination pursuant to Section 727 of the City of Oakland Charter is not required.

OWNER-CONTROLLED INSURANCE PROGRAM (OCIP)

This action is not subject to the Port's Owner Controlled Insurance Program (OCIP) as it is not a capital improvement construction project.

OPTIONS

1. Approve the *Amendment to Lease* with DHL Express (USA), Inc. as outlined above and authorize its execution by the Executive Director, which would (i) extend the term of the existing *Lease* by five years plus an additional five-year option; (ii) reduce the area of aircraft apron defined in the premises by 98,299± square feet and increase the rental rates for the warehouse and apron resulting in a net decrease in rental to $43,848 per month; (iii) approve a Security Deposit in the amount of $88,000 – based on DHL's excellent payment history to the Port – which is two-times the average monthly billings and an exception to Port Policy No. AP 509; (iv) change the maintenance provision in the *Lease* so that DHL would be responsible for maintaining the roof, skylights and exterior walls (in addition to the windows, doors and interior of the warehouse already required by the *Lease*); and, (v) require DHL to demolish the "Annex" structure and repair the underlying pavement by no later than June 30, 2018 at its sole cost and expense. This is the recommended action.
2. Do not approve the *Amendment to Lease* with DHL Express (USA), Inc. as outlined above, which could lead to DHL vacating the leasehold premises after the *Lease* expiration date of December 31, 2017, which would result in the facility being vacant and lost revenue of $43,848 per month. In the shorter term, assuming DHL remains on a month-to-month holdover basis, current rental of $66,062 would continue for a short time.
3. Do not approve the *Amendment to Lease* with DHL Express (USA), Inc. as outlined above but recommend different terms and conditions.

RECOMMENDATION

It is recommended that the Board give first reading to an ordinance to approve an *Amendment to Lease* with DHL Express (USA), Inc. and authorize its execution by the Executive Director, that would:

1. Extend the term of the existing *Lease* by five years to December 31, 2022, plus an additional five-year mutual option to extend the term to December 31, 2027 (both the Port and DHL would need to agree to the extension within 180 days of December 31, 2022);

2. Reduce the area of aircraft apron defined in the premises by 98,299± square feet from 115,859± square feet to 17,560± square feet;
3. Increase the rental rates of the warehouse from $0.587 PSF to $0.599 PSF and the apron from $0.196 PSF to $0.290 PSF, while leaving the land rental rate at $0.397 PSF, which will result in a total rental of $43,848 per month;
4. Approve a Security Deposit in the amount of $88,000 – based on DHL's excellent payment history to the Port – which would be an exception to Port Policy No. AP 509 which requires security deposits to be three-times monthly billings;
5. Approve changing the maintenance provision in the *Lease* which would require DHL to be responsible for maintaining the roof, skylights and exterior walls (in addition to the windows, doors and interior of the warehouse already required by the *Lease*); and,
6. Require DHL to demolish the "Annex" structure and repair the underlying pavement by no later than June 30, 2018 at its sole cost and expense (subject to separate permit and Board action).

All subject to the Port Attorney's review and approval as to form and legality.

ATTACHMENT "A"

SUMMARY OF TERMS – LEASE vs. PROPOSED AMENDMENT TO LEASE

DHL EXPRESS (USA), INC.

	Current Lease				**Proposed Amendment**			
Premises: Building L812 and adjacent vehicle and aircraft parking areas	Improvement		Square Feet		Improvement		Square Feet	
	Warehouse		39,555		Warehouse		39,555	
	Paved/Partially Paved Land		37,897		Paved/Partially Paved Land		37,897	
	Apron		115,859		Apron		**17,560**	
Term:	Ten (10) Years				Five (5)Years			
Option to Extend	None				**One Five (5) Year Mutual Option**[1]			
Commencement Date:	January 1, 2008				January 1, **2018**			
Monthly Rent:	**Improvement**	**Sq.Ft.**	**Rate**	**Rent**	**Improvement**	**Sq.Ft.**	**Rate**	**Rent**
	Warehouse	39,555	$0.587	$23,231.34	Warehouse	39,555	**$0.599**	**$23,693.45**
	Land	37,897	0.397	15,061.72	Land	37,897	0.397	15,061.72
	Apron	115,859	0.196	22,768.64	Apron	**17,560**	**0.290**	**5,092.40**
	Total Current Monthly Rent =			**$61,061.70**	**Total Proposed Monthly Rent =**			**$43,847.57**
Rent Adjustments:	Rent adjustments (upward only), every thirty (30) months by CPI.							
Security Deposit:	Equal to 3× monthly rent.				$88,000: Equal to **2x** monthly **billings (rent plus utility charges) rounded up to the nearest $1,000; conditioned on DHL's ongoing adherence to its exemplary payment record over the term of its occupancy.**[2]			
Option Term Rent Adjustment:	Not Applicable				**Rent shall be adjusted (upward only) based upon a Fair Market Rental Value (FMRV) appraisal**			

[1] "Mutual" Option to Extend Term; both parties must agree to the extension.

[2] Pursuant to Port Policy AP 509, security deposits "shall generally be equal to three months of average billings… amounts less than the three-month minimum standard must be approved by the Board…"

	Current Lease	Proposed Amendment
		process as described in the *Lease*.
Maintenance	Lessee is responsible for all Premises maintenance, except that Port shall be responsible for the repair and maintenance of the apron area, roof, skylights, and exterior walls of the Warehouse, but excluding windows, hangar doors and glass.	Lessee is responsible for all Premises maintenance **including the roof, skylights, exterior walls,** windows, warehouse doors and glass of the Warehouse (apron is removed from the Premises).
Port Capital Improvements	None	None
Lessee Capital Improvements	Design, construct and install improvements, fixtures and trade fixtures described on Exhibit F costing not less than $2,500,000.	**Demolish the "Annex" described on Exhibit F and restore and repair the Apron under the Annex[3] by no later than June 30, 2018**.
Employment Provisions	The Port's standard Equal Opportunity, Nondiscrimination Affirmative Action, and Prevailing Wage clauses effective as of January 1, 2008.	The Port's standard Equal Opportunity, Nondiscrimination, Affirmative Action, Prevailing Wage and similar employment clauses effective as of January 1, **2018**.

[3] DHL to either remove the Annex or place in escrow funds, an amount determined by the Port in its sole discretion, sufficient to fully reimburse the Port for its future costs to demolish the Annex. Approval of the *Amendment to Lease* does not approve the demolition; that will require separate approval and action by the Board.