

GROUND LEASE POLICY

CITY OF REDONDO BEACH - HARBOR ENTERPRISE

GROUND LEASE POLICY

The following paragraphs set forth the goals and objectives of the leasing policy of the City of Redondo Beach - Harbor Enterprise, together with specific policy guidelines.

I. STATEMENT OF GOALS

The primary goal of the City of Redondo Beach - Harbor Enterprise Leasing policy shall be to maximize the City's financial return from a valuable public real estate asset in a manner which (1) is consistent with land use patterns, the City's General Plan, the Harbor/Civic Center Specific Plan and structural improvements of which the City can be proud; (2) serves the broader recreational and economic needs of the community; (3) allows lessees to earn a fair return on their investments; (4) satisfies the City's fiduciary responsibility in the Tidelands as set forth in the State of California in the Grant of Trust; and (5) encourages high-quality development and operations to benefit the City and the community.

II. STATEMENT OF SPECIFIC OBJECTIVES

II.A Primary Objective

The primary objective of the lease policy is to set rent in a manner that simultaneously maximizes long-term revenues for the City and encourages and promotes effective development and continued entrepreneurial involvement by the lessees.

II.B Other Objectives

Other objectives of the lease policy are as follows:

1. to maintain meaningful control over the land uses, business methods and tenant quality of these leases in a manner befitting that of a public landlord rather than simply that of public regulation.
2. To fashion rental terms which effectively track the substantial increase in values that have been observed and are expected to continue with respect to waterfront and water-oriented property.
3. To establish lease terms, renewals and extension policies in such a manner as to encourage extensive rehabilitation and redevelopment as appropriate, notwithstanding the inherent problems of major capital investment associated with expiring land leases.
4. To assure that the City will receive the benefits of rising land appreciation but will not become a partner nor become directly

involved in operations, unless public policy so specifically mandates, since direct management responsibilities are inappropriate to its role as both a public regulator and a public fiduciary.

III. STATEMENT OF SPECIFIC POLICIES

Specific policies associated with ground leases fall into five major categories:

1. Term
2. Rent
3. Control
4. Financing and transfer
5. Other contingency clauses, (e.g. insurance and condemnation)

III.A Term

1. General Policy

The general policy of the City of Redondo Beach with respect to lease terms is that initial terms of all ground leases shall be as short as possible so as to accommodate the reasonable and fair financing for the improvements proposed.

2. Other Policy

The second policy with respect to term is that some effort should be given upon renewal to assuring that ground leases expire within as narrow a timeframe as possible. In this manner, releasing or other land use planning meeting the longer term needs of the City can be optimized.

III.B Rent

1. General Policy

The primary objective of the City's rental policy shall be to assure a regular and dependable flow of income that tracks the revenue productivity of the property. A parallel and equally important policy shall be a rental structure which, through percentage rent and participation in proceeds from sale or refinancing, also tracks the appreciation in the land value. The rent shall be structured to encourage the maximum revenues to the City through both lessee and sublessee performance and through the City's and lessee's choice of activity on the leasehold.

2. Classes of Rent

To implement this policy, there shall be four classes of rent:

- 2.(a) Interim, holding or construction rent at a reduced level during period of construction, redevelopment or other periods when the property is not fully productive.
- 2.(b) Minimum rent.

- 2.(c) Percentage rent based on gross revenues from lessee or sub-lessee operations.
- 2.(d) Appreciation rent in which the City receives some share of net proceeds from sale or assignment and refinancing of leaseholds.

2.(a) Interim Holding or Construction Rent

Interim, holding or construction rent shall be set at a fraction of minimum rent, typically .50% but not less than 25% of minimum rent.

2.(b) Minimum Rent

Minimum rent shall be set to provide an acceptable return leased on general market conditions on the fair market value of the improved leasehold land at the time the lease is initiated.

Minimum rent shall be adjusted at frequencies not less than every five years and by formula that either acknowledges some general price index or the reflection of the internal growth of total rents (minimum and percentage combined) from the lease.

2.(c) Percentage Rent

Percentage rents shall be based on gross revenue measurements rather than measurements of net revenue or net income. The number of percentage rent categories shall be minimized within the limits of providing a fair return to the City.

To the extent feasible within the context of the financing market, percentage rents shall be adjusted from time to time reflecting comparable market conditions and the changing contribution of land to total value that is not fully captured by simply rising total dollars as a constant share of revenue.

2.(d) Appreciation Rent

Appreciation rent shall be based on participation in net proceeds from a sale or assignment, and from a refinancing of a leasehold after allowing for recovery of lessee's total investment or payoff of existing financing.

There shall be provisions for excluding from the measurement of net proceeds those proceeds that represent approved capital reinvestment in the leasehold.

In general, participation rent should balance the City's share of land appreciation with the need to encourage reinvestment in the leaseholds.

3. Control

3.(a) Control of Uses

The primary policy with respect to control of uses is that the initial design of any new or reconstructed improvement shall be subject to the review of the City both in terms of its compliance and conformance to long-term revenue

goals and also with respect to the fact that the City as land owner must be assured of first quality and attractive design.

Within this policy, leases shall provide that, once an initial design has been approved, further reviews and approval of design shall be limited primarily to compliance with the initially approved design.

Parties to all City leases shall acknowledge that the City's control over land uses is in fact more restrictive and specific by virtue of its role as a landlord than by virtue as its role as regulator. Accordingly, leases shall have use clauses separate from and potentially more restrictive than those contained in zoning or general planning regulations.

3.(b) Control of Lessees

In addition to control over use, a key element of a public landlord is control over lessees. In order to ensure good reputation and, more important, continued revenue flow, Redondo Beach Harbor ground leases shall provide for restrictions on the right of transfer. These restrictions, however, shall not be unreasonable or arbitrary but shall deal among other items with reputation in and credentials, credit worthiness, demonstrated experience, and financial soundness of the proposed transfer or assignment.

4. Leasehold Financing

The City recognized that developers and lessees, in order to maintain the quality of improvements and maximize the revenue flow for both themselves and the City, must have access to long-term mortgage financing. In this context, the City shall endeavor to provide mortgagee protection (lender protection) provisions that are consistent with current practices and with the City's primary fiduciary objectives of maintaining an unsubordinated fee interest in the property.

Lenders shall not, however, be given the right to consent to lease change nor shall, as a matter of principle, the City agree to subordinate rent for the entire term of the lease. To the extent required by financing markets, subordination of portions of rent to initial financing, particularly in the case of reconstruction or development, may be considered.

5. Other Contingency Clauses

With respect to insurance and condemnation, the leases shall provide that normal patterns of distribution, recovery and liability shall apply subject to the fact that to the furthest extent possible in law or commercial reasonableness, the minimum flow of rent shall be maintained. Tenant shall be required to maintain rental insurance. In the event the projects cannot be reconstructed, provisions shall be made for the return of the property to the City in an orderly and appropriate basis. The lease shall contain appropriate covenants to ensure continuous operation of the leasehold barring force majeure events.

Damage and condemnation provisions shall specifically provide that, within 10 years of the projected expiration of a ground lease, there shall be some mechanism for a structured reversion of the property to the City with the

assurance that the lessee shall be reasonably compensated for the then appropriate value of the remaining leasehold.