

Memorandum

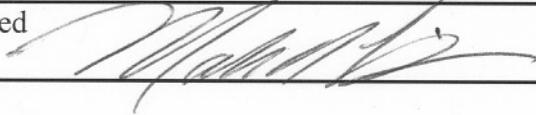
TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: Paul Krutko

SUBJECT: SEE BELOW

DATE: June 13, 2005

Approved



Date

June 23, 2005

COUNCIL DISTRICT: 3

SNI AREA: NA

SUBJECT: Approve the Selection of Imwalle Stegner as the Preferred Proposer to Develop Restaurant Services at the New City Hall Retail Space on 4th Street and the Proposed Business Terms, and Authorize the City Manager to Negotiate and Execute a Lease Agreement with Imwalle Stegner as the Master Tenant for the space.

RECOMMENDATION

It is recommended that the City Council:

- (a) Approve the Selection of Donald F. Imwalle, dba Imwalle Stegner, as the Preferred Proposer for the Master Tenant for the Development of Restaurant Service in the New City Hall retail space along 4th Street; and
- (b) Approve the proposed business terms to be included in the Lease Agreement for the space; and
- (c) Adopt a resolution authorizing the City Manager to Negotiate and Execute a Lease Agreement with Imwalle Stegner in accordance with the proposed business terms.

These actions further the vision of San Jose as the world's most livable big city, with diverse and distinctive qualities of life. "Develop Retail to Full Potential, Maximizing Revenue Impact and Neighborhood Livability." (Economic Development Strategy Initiative 13).

BACKGROUND

The New City Hall project establishes a new civic landmark in Downtown San Jose. The project includes approximately 6,000 square feet of retail space located on the Fourth Street side of the

**Approve the Selection of Imwalle Stegner as the Preferred Proposer to
Develop Restaurant Services at the New City Hall.**

Page 2 of 6

New City Hall. The selected tenants will serve nearly 1,700 City Hall employees, 1,000 City daily Hall visitors, and the broader Downtown community.

On April 15, 2005 a Request for Proposals (RFP) was issued for Food Services at the New City Hall. Staff advertised the RFP broadly, mailing out notices to Downtown businesses, area brokers and developers. Staff placed ads in the San Jose Business Journal, Mercury News, San Jose Post Record, El Observador, the Silicon Valley Chamber Newsletter, the Downtown Dimension and Small Business Chambers. The RFP was broadcast on the Vietnamese Chamber's radio program and e-mails were additionally sent to the Silicon Valley Chamber members. Staff held two mandatory pre-proposal conferences on April 28, 2005, at 9:00 am and at 6:00 pm. Approximately 25 different restaurants, brokers, and small businesses attended the combined pre-proposal conferences.

Five proposals were received by the May 27, 2005 due date. Two of the proposals were received later than the required 3:00 pm submittal time and were also otherwise not responsive to the minimum RFP requirements. The three responsive proposals included Imwalle Stegner, (A Real Estate Development Company), Starbucks Coffee Company, and Subway Sandwich and Salads. Imwalle Stegner submitted the original of a responsive proposal by the 3:00 pm specified deadline and later submitted 9 copies of the original at 3:25 PM. The later delivery of copies of the original proposal is considered by staff to be a minor irregularity and waivable. A committee of City representatives interviewed the three responsive respondents on June 13, 2005.

ANALYSIS

Request for Proposal Requirements

The New City Hall Request for Proposals (RFP) identified several key criteria:

- Provide a quality tenant mix that will enliven the New City Hall retail project and its environs.
- Demonstrate a strong financial capacity to ensure the ability to pay for the costs associated with the build out and operations of the space. The selected tenants or developer must accept the space "as is" and pay for all utilities and provision of required infrastructure, such as flooring and walls.
- Identify a California-licensed architect and contractor with a proven track record of successful retail project development.
- Show a quality design that complements the New City Hall and enhances food service Downtown core.
- Propose business terms that support successful project operations and provide a reasonable return to the City.

The RFP specified in detail that the retail space at new City Hall require substantial capital investment to bring it to "warm shell" condition.

Approve the Selection of Imwalle Stegner as the Preferred Proposer to Develop Restaurant Services at the New City Hall.

Page 3 of 6

Recommended Master Tenant/Developer and Proposed Subtenant Food Service Providers

Staff recommends that the Council approve the selection of Imwalle Stegner as the master tenant for development of the retail space. Imwalle Stegner (IS) has developed 75 retail projects, primarily in Santa Clara County, with 29 of the projects in San Jose. Mr. Don Imwalle led the effort to prepare the firm's response to the City's RFP. Mr. Imwalle has more than 30 years of experience in retail development. The vast majority of Imwalle's projects have been small buildings for food users and retailers. IS has relationships with a wide array of food service providers, affording the ability to select appropriate subtenants to maximize the opportunity for success at any given location. Many of the food service providers that IS works with are small and local businesses, creating projects that provide a unique dining experience.

Imwalle Stegner proposed that the New City Hall retail project include space for three subtenants, and proposed four possible subtenants to fill the three spaces. The selection of the final subtenant mix is subject to the conclusion of successful negotiations between Mr. Imwalle and the proposed subtenants. The food service providers recommended by Imwalle Stegner include:

- **Starbucks** – one of the world's premier coffee companies. Starbucks is well known for their fresh brewed coffee and specialty drinks.
- **Aqui**- located in Willow Glen - serves modern California cuisine with a Euro/Latin influence and plans to serve breakfast, lunch and dinner at the New City Hall. Aqui's incorporates a colorful and inviting interior and provides a wide variety of affordable entrees in a quick service format.
- **Three Dog Café** – is a new concept created by the founders of Aqui restaurant. Three Dog is envisioned to provide a bistro style café serving hand tossed salads, homemade soups, and grilled sandwiches.
- **Prolific Oven Bakery and Cafe** - currently located in Palo Alto, Saratoga, and Santa Clara, provides a wide array of products for breakfast, lunch, and dinner. The operation provides full bakery products in addition to affordable menu selections.

In the unlikely event that Imwalle Stegner is not able to conclude with three of the four proposed subtenants identified above, Imwalle has the ability to recommend alternative tenants as substitutes. The RFP and the proposed lease require the City's approval for substitution of subtenants.

Imwalle Stegner's proposal provides strong responses for each of the desired criteria in the RFP. Keyser Marston Associates, advisors in real estate, economics, and redevelopment was hired by the City to review the financial submittals of all proposers. Tim Kelly of Keyser Marston indicated that Imwalle has provided financial documentation assuring sufficient funds to execute the project successfully. Additionally, as stated previously, Imwalle has completed numerous

**Approve the Selection of Imwalle Stegner as the Preferred Proposer to
Develop Restaurant Services at the New City Hall.**

Page 4 of 6

retail projects in San Jose and Santa Clara County demonstrating the firm's ability to construct, operate, and maintain the type of retail space envisioned in the New City Hall retail project.

The RFP also sought to ensure that other important criteria were met through the project including:

- Payment of prevailing-wages in the construction phase of the project.
- Provision of labor peace requirements by selected tenants.
- Opportunity for small and local businesses to participate the project.

Imwalle Stegner's proposed proforma includes construction costs that accommodate prevailing wages throughout the construction of the project. Imwalle has assured City staff the firm has already discussed labor peace requirements with the proposed tenants and that all selected tenants will have appropriate labor peace processes in place at lease signing. As mentioned earlier, Imwalle regularly works with several small and local tenants based in Santa Clara County. The RFP requested that the tenants of the New City Hall retail space include at least one small and local tenant. The final mix of tenants will include at least one small and local food service provider.

Proposed Business Terms

In addition to the foregoing terms included in the RFP, the RFP included an exemplar lease agreement with standard provisions acceptable to the City, with business, construction, and operation issues subject to negotiation between the City and the successful proposer. The RFP provided, as will the lease, that the premises are accepted "as is" and are to be brought from "cold shell" to "warm shell" by the Developer. The RFP and the lease also provide that the premises will be leased on a triple net basis, with no additional City financial obligations for utilities, maintenance, possessory interest taxes, brokerage fees, and other costs or expenses.

Imwalle Stegner accepts the City requirements and has proposed the following business terms:

- 25 year term of lease, one 10 year option to renew
- An estimated Tenant Funded improvement budget of \$1,350,000 of which \$978,841 is construction cost
- Rent Commencement 180 days from lease signing
- Proposed annual rentals:
 - a. Years 1-10 \$35,000 per year (\$5.57 per sq.ft per year)
 - b. Years 11-15 \$130,000/year (\$20.71 per sq.ft per year)
 - c. Years 16-20 \$143,000/year(\$22.78 per sq.ft per year)
 - d. Years 21-25 \$157,000/yr (\$25.00 per sq.ft per year)

**Approve the Selection of Imwalle Stegner as the Preferred Proposer to
Develop Restaurant Services at the New City Hall.**

Page 5 of 6

Based upon the financial analysis from Keyser Marston and the substantial capital investment involved in build out of the space, staff believes that the proposed rental rates are reasonable but that in year 11 forward of the proposal, some negotiation may be appropriate to determine whether greater returns to the City are achievable. The staff shall negotiate appropriate language with Imwalle Stegner.

Staff also prefers that Imwalle Stegner hold the leasehold as the long term Master Tenant, and that the City have authority to review and approve any assignee in order to assure that any successor would have the financial capacity and the ability to draw quality food service subtenants. The conditions under which a change in the Master Tenant would be considered will be included in the negotiations and the lease agreement.

Imwalle Stegner has indicated that one of its proposed subtenants, Aqui, wishes to sell alcoholic beverages on the premises. The Office of Economic Development recommends allowing appropriate tenants in the project to sell alcoholic beverages on site, if the tenant obtains all necessary approvals. The retail spaces along 4th Street, though a part of the new City Hall, are oriented to serve the general public at a range of hours, and not intended solely for use by City employees. Staff is recommending that the proposed lease not preclude the sale of alcoholic beverages. The City Attorney's Office recommends inclusion of appropriate hold harmless and indemnification provisions to protect the City from liability for any such sales. It would be up to the Developer to obtain all necessary state or local regulatory approvals, including any required City permits or other regulatory approvals, to permit such sales in the restaurant.

Staff requests that Council approve the proposed business terms and give direction to negotiate a final lease document consistent with the terms described above, with the understanding that the specific rental rates proposed may be adjusted through a defined negotiation process prior to the eleventh year.

Alternative Proposals

The other respondents to the RFP included Starbucks Coffee Company and Subway Sandwich and Salads. Starbucks is very interested in the New City Hall location. The company wanted to ensure its participation in the project by submitting proposals both as a participant in Imwalle's team and as an individual tenant. Amita and Benikan Sheth operate the successful Subway franchise located at 165 West San Fernando Street. Mr. and Mrs. Sheth propose to provide limited tenant improvements only after a developer provides substantial improvements such as the provision of utility services, fire sprinklers, and flooring. Mr. and Mrs. Sheth are not prepared to accept the space "as is", and bring it to warm shell condition.

Honorable Mayor and City Council
June 22, 2005

**Approve the Selection of Imwalle Stegner as the Preferred Proposer to
Develop Restaurant Services at the New City Hall.**

Page 6 of 6

OUTCOMES

The selection of Imwalle Stegner will result in quality food service at the New City Hall. The respondent has the demonstrated ability to provide quality, healthy and affordable menu choices for the benefit of City Hall employees and visitors in addition to area workers and residents. Imwalle Stegner also has the financial, construction, and operational experience to ensure effective management and operation of the New City Hall Retail space.

PUBLIC OUTREACH

As mentioned above, the New City Hall Retail RFP was advertised broadly to area businesses, brokers, and developers. Several advertisements announcing the RFP were placed in area news outlets and e-mail notification was provided to area businesses.

COORDINATION

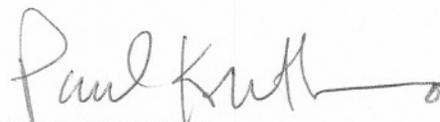
This memorandum has been coordinated with Public Works, the Redevelopment Agency, General Services and the City Attorney's Office.

COST IMPLICATIONS

As a condition of the lease to be negotiated between the City of San Jose and Imwalle Stegner, the respondent will assume all costs associated with the build-out and maintenance of the New City Hall Retail space. No costs for the project are attributed to the New City Hall budget.

CEQA

Civic Plaza Environmental Impact Report, Resolution 68905



PAUL KRUTKO
Director, Office of Economic Development