



COUNCIL AGENDA: 9-11-2007
ITEM: 2.3

Memorandum

TO: HONORABLE MAYOR AND
CITY COUNCIL

FROM: William F. Sherry, A.A.E.

SUBJECT: SEE BELOW

DATE: August 20, 2007

Approved

Deanna Antna

Date

8/20/07

COUNCIL DISTRICT: Citywide

SUBJECT: FIRST AMENDMENT TO THE LEASE BETWEEN THE CITY OF SAN JOSE AND SKY CHEFS, INC.

RECOMMENDATION

Approval of a First Amendment to the Lease Agreement between the City of San Jose (City) and Sky Chefs, Inc. (Sky Chefs), to change the Base Rental for non-airline, off-Airport sales activity to 0% of gross receipts for the period of January 1, 2008 through December 31, 2008, and 2% thereafter.

OUTCOME

Should Council approve the Amendment, the City will receive a lower concession fee for goods produced for non-airline, off-Airport sales. In return, Sky Chefs has indicated that they will increase the sales of these goods which will add to the City's total gross receipts. In addition, Sky Chefs will replace a non-functioning autoclave, which will save the City \$800,000 in this fiscal year.

BACKGROUND

Sky Chefs' has operated an in-flight catering kitchen under the terms of a Lease Agreement dated May 9, 1995, which will expire in 2016. The Lease provides as consideration a percentage fee of 10% on gross receipts or a Minimum Annual Guarantee (MAG), whichever is greater. The definition of gross receipts includes all sales generated on-Airport regardless of type of business or ultimate destination of the product.

Sky Chefs gross revenues have declined significantly from a high of \$24.9 million in FY 2000-2001 to \$6.8 million in FY 2006-2007, which represents a 73% decrease. The MAG is adjusted each year to an amount equal to 85% of the previous year's payments to the City but in no case will it be reduced below \$500,000 per year. Sky Chefs has been paying only the MAG since

sales dropped in 2002, as the MAG has been higher than the percentage rent. The MAG for 2001-2002 was \$1,858,430 and has steadily declined annually to \$911,248.56 for FY 2007-2008.

ANALYSIS

Sky Chefs has suffered a considerable reduction in income since September 11, 2001, as airlines have eliminated in-flight meals and international traffic at San Jose has declined. In an effort to reduce costs, Sky Chefs has requested and been granted similar reductions in off-airport, non-airline percentage fees at other airports across the country including Boston, Fort Lauderdale, Tampa, Orlando, Kansas City and Salt Lake City.

Sky Chefs has requested to move their off-airport retail catering operation into their on-airport facility and pay a lower percentage rent for this activity. This could increase revenue to the City by capturing sales that are currently generated out of Sky Chefs' off-airport location. The agreement with Sky Chefs provides that they may cater off-airport provided the activity does not interfere with airline related activity.

The Airport has negotiated with Sky Chefs to pay no Base Rental on the off-Airport retail catering for one year and 2% thereafter. This will allow Sky Chefs one year to establish itself further into the off-airport market and provide time to consolidate its operations. The formula for the calculation of the MAG would remain unchanged and the total MAG would not drop below \$500,000 per year.

In addition to the Base Rental adjustment, staff has negotiated with Sky Chefs to require that they provide and maintain an autoclave on-site to handle international trash as required by the United States Department of Agriculture. Without this autoclave, the City would need to purchase, operate and maintain the unit to provide this service to the airlines in order to continue international passenger traffic at the Airport.

EVALUATION AND FOLLOW-UP

The Director of Aviation shall be responsible for coordination of this Agreement and shall render overall supervision of the progress and performance of this Agreement.

PUBLIC OUTREACH/INTEREST

- Criteria 1:** Requires Council action on the use of public funds equal to \$1 million or greater. **(Required: Website Posting)**
- Criteria 2:** Adoption of a new or revised policy that may have implications for public health, safety, quality of life, or financial/economic vitality of the City. **(Required: E-mail and Website Posting)**

- Criteria 3:** Consideration of proposed changes to service delivery, programs, staffing that may have impacts to community services and have been identified by staff, Council or a Community group that requires special outreach. **(Required: E-mail, Website Posting, Community Meetings, Notice in appropriate newspapers)**

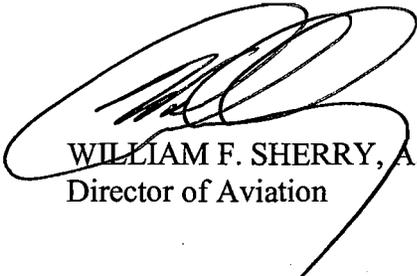
This item does not appear to qualify as an item of significant interest based on the established criteria. This memo is posted on the City's website for the August 28, 2007 Council Agenda.

COORDINATION

This memo has been coordinated with the City Attorneys office and the Public Works Office of Equality Assurance.

CEQA

CEQA: Exempt, ND (Negative Declaration) or Resolution Nos. 67380 and 71451, PP 07-155.


WILLIAM F. SHERRY, A.A.E.
Director of Aviation

Please direct questions to William Sherry, Director of Aviation, at (408) 501-7669.