TO: HONORABLE CITY COUNCIL

FROM: CITY MANAGER     DEPARTMENT: ADMINISTRATIVE SERVICES

DATE: JULY 19, 2004     CMR: 350:04

SUBJECT: AWARD OF OPTION TO LEASE TO CRIMSON PALATE, INC., D.B.A. SAFFRON CLUB RESTAURANT AT LOT S/L SITE NON-PARKING AREA, 445 BRYANT STREET

RECOMMENDATION

Staff recommends that Council authorize the Mayor to execute the attached option to lease with Crimson Palate, Inc., d.b.a. Saffron Club Restaurant, for the 7,410 square foot office/retail space in the non-parking area of the Lot S/L site, 445 Bryant Street.

BACKGROUND

On March 19, 2001, Council approved a new University Avenue Off-Street Parking Assessment District to provide funding to design and build two new parking structures on Lots R (High/Alma South Garage) and S/L (Bryant/Florence Garage). In addition to building a parking structure on the Lot S/L site, Council approved construction of a non-parking area that would be an extension of the parking garage. Costs for building the extension were to be paid from Certificates of Participation (COP) backed by the City’s General Fund. Initial plans for this area were for a downtown teen center, with the remaining space to be used for rental and other commercial purposes. Rent from commercial users was to be used to offset the City’s debt service costs for constructing the non-parking area.

On May 14, 2001, as a result of receipt of the Youth Master Plan study and a student survey indicating teens would prefer having more programs, activities and special events to a new downtown teen center, Council approved a staff proposal endorsed by the Youth Council to allocate 75 percent of net revenues derived from renting the entire non-parking area to funding youth and teen activities and the Barker Hotel parking assessment. On December 10 and December 17, 2001, Council reviewed and approved
the financing for construction of the non-parking area on the Lot S/L site. Construction of the non-parking area was completed in February 2004.

DISCUSSION

Non-Parking Area Office/Retail Space
The non-parking area space for lease totals 7,410 square feet, consisting of two 3,705 foot floors of open bare space ready for a tenant to build to suit. The space is divisible to 1,500 square feet, and the zoning allows for ground floor retail and second floor office or retail. During the design process, Council specified the uses that would be permitted under the Ground Floor Combining District (GF) were: 1) eating and drinking; 2) personal services; 3) retail services; and 4) travel agencies. Financial service providers are not allowed nor are any conditional uses.

As discussed in the May 10, 2004 City Manager’s Report to Council (CMR:253:04), the non-parking area of the Lot S/L garage was constructed for less than the budgeted cost, leaving $1 million remaining in bond proceeds. Some of these remaining funds will be used to pay for shell improvements, such as the heating and air-conditioning system (HVAC) and sprinkler system, in order to assure the equipment installed will be dependable and the easiest for the City to maintain. In CMR:253:04, staff estimated the City’s cost for tenant improvements would be a maximum of $40-$50 per square foot ($296,400 to $370,500) of the total tenant improvements of $80-$100 per square foot ($592,800-$741,000). The City will be responsible for maintaining the outside of the building, the roof, the heating and air-conditioning system (HVAC), sprinkler system and elevator. The tenant will be responsible for all other maintenance, taxes and insurance.

Solicitation of Proposals
Staff began advertising the space for lease in early April 2004. Advertising included placing “For Lease” signs in the windows of the buildings to be leased and mailing over 250 brochures to local commercial real estate brokers and agents informing them of the availability of the space.

Proposals were received until 5:00 p.m. June 9, 2004, by which time six written proposals were submitted. Two of the six proposals are to lease the entire 7,410 square feet of space and four propose to lease varying portions of the space. The proposals are summarized as follows and in Attachment A: 1) The Saffron Club Restaurant (Saffron Club), proposing a 10-year lease for the entire space with an initial rent of $3.00 per square foot and a City allowance of $40 per square foot for improvements (tenant to pay for any improvement costs over $40 per square foot); 2) a health and fitness service, proposing a 10-year lease for the entire space with an initial rent of $1.85 per square foot and a tenant improvement contribution of $10 per square foot; 3) a restaurant proposing a 10-year lease for approximately 5,650 square feet with a rent of $2.50 per square foot; 4) a wine tasting
and retail sales use proposing a 3-year lease for 1,500 square feet at $3.00 per square foot; 5) a printing use proposing a 5-year lease for 1,100 square feet at $3.00 per square foot; and 6) a beauty salon proposing a 3-year lease for 1500 square feet at $3.00 per square foot.

Evaluation of Proposals
The primary factor staff used in evaluating the proposals is lease income to the City. In its December 10, 2001 report to Council regarding the financing of the construction of non-parking space on Lot S/L (CMR: 444:01), staff estimated rental rates would come in at approximately $4.50 per square foot rent for the second floor office space and $5.00 per square foot rent for first floor retail space. This amount would have covered the projected annual debt service payment on the taxable COPs of around $331,000, leaving net revenue of $131,000 to partially offset the Barker Hotel parking assessment; for youth and teen services; and for General Fund revenue. However, since the 2001 staff estimates, the market for office/retail space has weakened, and the rentable square footage is actually less than originally thought. Of the six proposals received, the highest per square foot rental proposed is $3.00. If the entire site is leased for $3.00 per square foot, the annual rent would be $266,760, far less than the 2001 projected rent of $462,000. Although the actual annual debt service payment for the S/L lease space COPs is $320,000 (less than the $331,000 projected in the 2001 staff report), it would require a rent of at least $3.60 per square foot per month to cover the annual debt service payment.

Attachment A compares the six proposals in terms of proposed square footage, lease term, rent per square foot and contribution to tenant improvements. Of the six, the Saffron Club proposal results in the highest income to the City. The Saffron Club’s proposed 10-year lease for the entire 7,410 square feet of space, with a $40.00 per square foot City allowance for improvements and a rent of $3.00 per square feet in the first year and increasing to $4.20 in the 10th year, results in a total income to the City of $3,173,202 over the 10-year term. By the 6th year of the lease term, the rent will be $3.61 per square foot, enough to cover the annual debt service payment for the COPs. The total income to the City from the proposed Saffron Club lease exceeds the income from next highest proposal by $370,000.

As described in its proposal, the Saffron Club is an upscale contemporary fusion South Asian restaurant and wine bar, which Crimson Palate, Inc. will open in key urban clusters in the United States. The proposed restaurant will be the flagship unit and the leased space will also house the company headquarters. The full-service restaurant will be open for lunch and dinner six days a week and will include a delivery/takeout menu. The restaurant will offer high quality, fresh South Asian food in a modern setting with the cuisine to be developed by nationally renowned chefs, led by Chef Floyd Cardoz of Tabla Restaurant in New York City who has won numerous national culinary awards. The Saffron Club plans to promote and showcase the work of local artists within the
restaurant and to hold exhibitions and events regularly to exhibit the work of small, unknown artists who generally do not have the opportunity to display their work in a retail setting. The restaurant anticipates being a destination restaurant for both Palo Alto residents and residents of other towns and acting as an anchor to attract people and new businesses to the neighborhood. Saffron Club Restaurant was oversubscribed in its fundraising, which has been completed and will be used to finance tenant improvements and initial operations. The restaurant has strong financial backing and stable investors in place who are committed to the long-term financial success of the restaurant.

Total tenant improvements for the Saffron Club are estimated to cost $120 to $150 per square foot ($889,200 to $1,112,000). The City will contribute up to $40 per square foot ($296,400) for items such as the HVAC, sprinkler system, grease trap, electrical upgrade and ADA compliant restrooms. The Saffron Club will be responsible for all costs above $40 per square foot.

Option to Lease
Based on its evaluation of the proposals, staff has negotiated the attached option to lease with Saffron Club. Terms of the option and lease are summarized in Attachment B. Under the option agreement, the Saffron Club is granted a nine-month period to satisfy the specified conditions prior to exercising the option and entering into the lease. The major conditions the optionee must satisfy:

1. Pay the option purchase price ($5,000).
2. Receive approval of its improvement plans from the Architectural Review Board and receive approvals from the City Engineer and Chief Building Official of the construction drawings, including the construction contract form and proposed construction schedule.
3. Receive approval of any and all permits required to implement the proposed use and improvements.
4. Satisfy the Director of Administrative Services that optionee has sufficient finances or financial commitments to implement the project as approved by the City and furnish the Director of Administrative Services with evidence that sufficient financial security will be available to construct the project.
5. Submit to the Real Property Manager a security deposit as required by the Lease.

Once the option conditions are met, the lease will be executed by both parties without returning to Council. Major terms of the lease include a 10-year term with two 5-year options to renew; a rent of $3.00 per square foot in the first year, increasing to $4.20 by the tenth year; tenant to pay for all improvement costs above the City’s $40 per square foot contribution; City to maintain roof, HVAC, sprinklers and elevator; tenant to be responsible for all other maintenance and cost of annual maintenance inspection.
contracts; tenant to pay for utilities, insurance and taxes and assessments; and assignments and subletting subject to City approval.

**RESOURCE IMPACT**

The City’s cost for structural improvements will be $296,400, to be paid from the $1 million remaining in bond proceeds from the construction of the non-parking area of the Lot S/L garage. Staff is in the process of evaluating whether to use remaining COP proceeds to retire certificates or offset annual debt service.

Total rental income to the City over the 10-year term of the proposed lease will be $2,876,802. In addition, staff estimates the tenant will generate between $14,800 and $18,000 in annual sales taxes. For the first five years of the lease, the rental income will be used to partially offset the $320,000 annual debt service payment on the taxable COPs used to construct the non-parking space on Lot S/L. Starting with the sixth year of the lease, the rental income will be adequate to pay the entire COP annual debt service, with any excess rental income to be used to partially offset the Barker Hotel parking assessment; for youth and teen services; and for General Fund revenue.

**POLICY IMPLICATIONS**

The proposed option to lease does not represent any changes to existing City policy.

**ENVIRONMENTAL REVIEW**

An Environmental Impact Report for the parking structures, including the non-parking area, was prepared as part of the zoning application and was certified by Council on December 20, 2000, by adoption of Resolution No. 7917. During the option period, the optionee will be required to fully comply with all provisions of CEQA as they may apply to improvement plans.

**ATTACHMENTS**

Attachment A: Proposal Spreadsheet  
Attachment B: Summary of Option to Lease  
Attachment C: Option and Lease

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