TO: HONORABLE CITY COUNCIL

FROM: CITY MANAGER    DEPARTMENT: COMMUNITY SERVICES

DATE: NOVEMBER 17, 2008    CMR: 446:08

REPORT TYPE: STUDY SESSION

SUBJECT: Operational Analysis of the City Palo Alto Municipal Golf Course

EXECUTIVE SUMMARY
In 2007 the City Council authorized staff to proceed with an operational analysis of the Palo Alto Municipal Golf Course (“Golf Course”). The operational analysis (Attachment A), was conducted by Economics Research Associates (ERA), and provides information on the Bay Area golf market and conditions of the Golf Course facility; and the current and alternative operating models available for the Golf Course. The study found that, despite a Bay Area wide decline in golf play, the Golf Course performance has been relatively strong when compared with similar municipal facilities in the market area.

The ERA study and staff report recommends several actions for future success of the Golf Course, which includes: making relatively minor but strategic investments in the Golf Course infrastructure and operating structure along with actively participating in the planning of flood control alternatives for San Francisquito Creek to find a balanced flood control / recreational use solution that would benefit the Golf Course. Additional recommendations include aligning tenant contracts to expire concurrently and to evaluate options to enhance Golf Course maintenance, including the advantages and disadvantages of private versus public maintenance. Various Golf Course operating models are described in the ERA report, each with advantages and disadvantages. In the short term, no recommendation is proposed to alter the current operating model until the flood control plans for San Francisquito Creek, which may impact the Golf Course, are clearly defined.

Staff is presenting this report to Council for information and preliminary feedback. This item will be placed on the Finance Committee agenda in the future for further discussion and recommendations to Council.

BACKGROUND
The Golf Course was constructed in the mid 1950’s on 184 acres of flat former salt-marsh and bay fill. The course was designed by noted golf course architect William R. Bell of Pasadena, California. The Golf Course was designed as an 18-hole facility with a par of 72. The Golf Course is a classic 18-hole championship course that measures over 6,800 yards from the back
tees. The facility includes a large practice putting green, a three-building Eichler-designed-clubhouse/golf shop complex and parking lot. In the mid 1970’s, improvements were made to replace the clubhouse buildings. At that time, holes 3, 10, 11, & 18 were renovated under the direction of golf architect Robert Trent Jones, Jr.

In 1992, the City Council initiated a Master Improvement Plan process (CMR 453:92) for the Golf Course that would incorporate the findings of all prior studies, as well as look to the future for necessary improvements to the aging facility. The firm of Halsey Daray Golf was selected to prepare the Master Plan. Subsequently, in 1998, Certificates of Participation (COP’s) were issued in the amount of $7,750,000 (CMR 357:98) to fund the master plan improvements, and work commenced on the driving range, fairways, greens and tees in 1999. Due to escalating project costs and funding limitations to make the annual debt service payment the COP issuance only addressed 40 percent of the proposed master plan improvements.

The Golf Course is a City of Palo Alto General Fund operation. All excess revenues or shortages are returned to the City’s General Fund. The Golf Course currently generates sufficient revenues to support debt service, direct and indirect expenses, and City cost plan charges. There is no reserve or replacement fund for the Golf Course, consequently; additional debt service is taken on by the Golf Course when new capital improvement needs arise. The debt service for the COP’s, which represents approximately $570,000 annually, will be fully retired in 2018.

Presently, the City has a management agreement and a lease agreement with Brad Lozares for golf operations. As a result of Internal Revenue Services (IRS) debt issuance limitations, the management agreement and the lease for the building are separate contracts. The management agreement includes the following responsibilities: reservations; green fees collection; starting; and marshalling services. The lease agreement for the building includes responsibility for: managing golf cart rentals; the driving range; merchandise sales; and instruction services. Mr. Lozares’s management agreement with the City for operating the Golf Course expires December 31, 2009. The lease agreement with Mr. Lozares for lease of the building expires in April 2013; the building lease also includes an option to extend the term of the concession 10 additional years, if the option is exercised at the City’s sole discretion.

There is also a lease agreement with R&T Restaurant Corporation (R&T) for food and beverage services at the Golf Course. The R&T lease agreement for food and beverage operations expires April 20, 2018.

Golf Course turf and irrigation maintenance is provided by the City’s Community Services Department, Recreation and Golf Division. The Club House and Pro Shop building maintenance (exterior) and janitorial services are provided by the City’s Public Works Department, Facilities Management Division.

The Recreation and Golf Division Manager of the Community Services Department oversees daily operations that include coordination of services between the tenants and City maintenance staff in order to provide a seamless experience for visitors to the Golf Course. The Real Estate Division of the Administrative Services Department oversees tenant leases.
Faced with increased competition in the regional golf market, challenges in the golf facility physical product, and increased pressure on City finances, a study was conducted at the request of former City Manager Frank Benest, and funding was approved as part of the 2007 budget process, with the following two key objectives:

a) provide analysis on the Bay Area Golf market and conditions of the Golf Course facility; and

b) provide analysis of the current and alternative operating models available for the Golf Course.

In 2007, a scope of services was developed and an RFP process followed to retain a consultant to conduct the analysis. Economics Research Associates (ERA) was selected for their reputation in the industry, experience conducting comparable studies for similar golf courses, excellent references and reasonable fee proposal that met the City’s budget for the project.

DISCUSSION

The ERA report (Attachment A) provides detailed information regarding the Golf Course that will help put into context how the Golf Course has performed in recent years in comparison to nearby courses, along with recommendations and options for future success of the Golf Course.

Extensive public outreach was undertaken to capture the views and interests of stakeholders. Among them were the Golf Advisory Committee, members of the Parks and Recreation Commission, golfers who frequent the Golf Course, interested residents, and Baylands enthusiasts, among others. A Golf Course survey was available at the course for six weeks and 2,500 surveys were mailed to golfers who frequent the Golf Course; 454 responses were received and are summarized in the ERA report (Section V).

The study concludes that the Golf Course, as with others in the region, has been negatively impacted by market forces over the last decade. With the entry of many new public and private golf courses in the region, the market has become significantly more competitive. Due to this extraordinary golf course inventory expansion, along with a downturn in the regional/national economy, comparable Bay Area golf courses, on average, report a 17% decline in annual rounds played from 2000 to 2007. The Palo Alto Golf Course has experienced a 16% decline in annual play during this period. Sound management decisions, cooperation among the tenants, loans from the General Fund, strategic maintenance choices and enhanced marketing have enabled the Golf Course to continue to recover the costs of operations, fund related debt service, and to cover City and Community Services Department (CSD) allocated overhead charges (Cost Plan). The study points out that, despite the decline in play at the Golf Course, the operating performance has been relatively strong compared to similar municipal facilities.

There are several options for the future of the Golf Course, each with its own set of challenges and opportunities. The long term Golf Course operating models that the City may want to consider include: Facility Lease; Management Agreement; City Self Operation; or a Hybrid Model such as the City has currently. The advantages and disadvantages of these options are described in Section VI of the ERA Report.
In the near term, the choices for Golf Course improvements and/or changes to the operating model, which the City may wish to consider, will likely be influenced by the results of the pending flood control plans for San Francisquito Creek, being conducted by the Joint Powers Authority and the Army Corps of Engineers.

Consequently, below are three alternatives to help spur discussion on the future of the Golf Course, with a focus on the possible impacts and opportunities the flood control plans for San Francisquito Creek may present.

A brief summary of three possible alternatives for moving forward are discussed below:

I. Make no changes, and work with the Joint Powers Authority (JPA) for San Francisquito Creek flood control to minimize Golf Course impacts

The flood control plans for San Francisquito Creek, being conducted by the Joint Powers Authority and the Army Corps of Engineers, has begun with the key objective of identifying potential options to reduce flooding along the creek. A list of short-term projects will be complete as early as 2010, with the possibility of breaking ground on an actual project by summer of 2011. The flood control plans for San Francisquito Creek remain an important factor in planning for changes and improvements at the Golf Course because the creek is adjacent to the Golf Course and, at one time, traversed the land occupied by the course. Some of the recommendations that come out of the flood control study may necessitate modification of portions of the Golf Course. One course of action may be for the City to work with the Joint Powers Authority to find flood control solutions that have minimal to no impact on the Golf Course.

The ERA report states that the Golf Course operating performance is satisfactory, particularly in light of a very soft Bay Area golf market. Within the short term, two to three years, the operating performance will likely remain stable with no significant change to the operating structure or major investment in capital improvement to the Golf Course. The study does not identify any urgent capital improvement needs or operational problems that need to be addressed in the short term. On the contrary the Golf Course, as compared to the key competition, is performing better than average. Given this fact, it is not unreasonable to, at least for the short term, make no significant changes.

II. Actively participate in the planning of flood control alternatives for San Francisquito Creek, to explore possible balanced flood control / recreational use solutions that would benefit the Golf Course; and pursue strategic operational modifications and Golf Course improvements as outlined in the ERA Report

This alternative is most consistent with the ERA report and is also the alternative that staff believes to be the most prudent at this time. The goal would be to optimize financial performance through some strategic investments while working closely with the Joint Powers Authority on a flood control project for San Francisquito Creek that will enhance the golf course. The specific actions under this option would include the following:
- Retain a golf course design consultant to work with the Joint Powers Authority and City staff to design an environmentally friendly flood control project that will
balance flood control and recreational use solutions and also benefit the Golf Course.

- Align the two tenant leases and management contract so they expire concurrently. This would allow consideration of other, potentially more effective and efficient, operating options and a smoother transition of operation, should that be deemed advantageous in the future.
- Commit to a plan of cost neutral capital improvements, as outlined in the study (summarized on page I-12), to ensure the Golf Course remains competitive. That is, proceed with improvements that are economically justified by increased net operating income stemming from the improvements.
- Recalculate the Cost Plan allocation for the Golf Course to a more traditional golf course operation allocation. This would allow for excess funds to be set aside to establish a replacement reserve to fund ongoing minor capital improvement and/or more intensive maintenance.
- Direct Community Services and other relevant City staff to further evaluate the advantages and disadvantages of private versus public maintenance. The City will meet and confer with the union on any labor issues which arise.

III. Embark on a significant redesign of the Golf Course with or without a concurrent restructuring of the Golf Course operation that takes advantage of possible flood control funds that may become available

The ERA report finds that the Golf Course is presently operating at a satisfactory level with respect to cost recovery and annual rounds of play as compared to other comparable golf courses in the region, and can be maintained as such with minimal additional investment. However, if the City aspires to build or move toward developing a true destination or signature golf course, a new vision would need to be formulated. This could take several forms. For example, significant design changes to the course could reflect more of a links-style course with wide-ranging natural wetland grasses and round contours that provide undulations and slopes for a more unique golfing experience. Another concept could be to extend the lake on hole 11 through the fairways on holes 3 and 18 to create two or more signature holes. These would be unique, challenging holes that would bring golfers back to play again. Moreover, this concept may include partnering with an entrepreneur to build and operate a destination restaurant, one that overlooks the 18th hole and vistas of the airport; a restaurant with a character and ambiance to attract residents to take out of town visitors to dine.

Several members of the community share this vision in one form or another. They believe that with the right people and investment, it is possible to create a better Golf Course that has a unique design, providing a long term competitive advantage in the market place. A significantly enhanced Golf Course, coupled with a destination restaurant, could be a successful strategy. Although this is a compelling vision, funding a comprehensive re-development project at the Golf Course, even with possible flood control funds, would be very challenging, particularly in the current economic environment.
Related to the idea of a comprehensive Golf Course redesign, at Council’s direction, staff has investigated the possibility of re-designing the Golf Course in order to create room for playing fields (CMR 168:06). This concept was extensively studied by the Planning staff and also explored by the Parks and Recreation Commission. In 2006, City staff and the Parks and Recreation Commission concluded that the concept of playing fields at the Golf Course should be deferred until the flood control options become more certain. Creating new playing fields could be re-investigated as part of a comprehensive re-design but again this would add additional expense which would be particularly challenging in the current economic environment.

**Staff Preferred Alternative**

At this time, staff recommends pursuing Alternative II. This alternative entails making relatively minor but strategic investments in the Golf Course infrastructure and operating structure as outlined in the ERA report along with actively participating in the planning of flood control alternatives for San Francisquito Creek.

The goal would be to find a balanced flood control and recreational use solution that would both improve creek flood control and benefit the golf course. Joint Powers Authority flood control concepts include the Golf Course and provide a unique opportunity for possible Golf Course enhancement if the City actively participates in the design and development of the project.

With regard to strategic investments in the Golf Course infrastructure and operating structure, prior to the most recent economic downturn the golf market was expected to remain relatively stable for the next three years, the current economic conditions will likely present new challenges in maintaining a stable level of play. Although the Golf Course is performing reasonably well today, staff believes maintaining the status quo (Alternative I) is too passive a strategy in a market that is increasingly competitive and dependent on discretionary income. Given the current economic climate, it is imperative to commit to strategic investment in course improvements and maintenance practices to ensure the City is providing the best possible golfer experience. This will maintain or improve the City’s place in the market and enable the City to reach cost recovery targets.

Moreover, minimal cost neutral capital improvement, enhanced marketing such as the implementation of online reservations and better course maintenance are all needed to ensure long term success. Alternative III, which paints a more dramatic picture of change and redesign of the Golf Course is a compelling option and remains possible. This option can be preserved by addressing the issues of aligning contracts and lease expiration terms and addressing the advantages and disadvantages of private versus public maintenance as outlined in Alternative II. It also keeps open the potential for a more comprehensive re-design project that may have additional recreational benefits such as adding playing fields.

**RESOURCE IMPACT**

Working with the JPA on a flood control / enhanced Golf Course design project will require Community Service staff input, golf course design expertise, and public input. Golf course design expertise may require consultant costs.
In an attempt to maintain the standard cost allocation plan across City departments staff recommends that, after further analysis by the Administrative Services Department, any reduction in City Cost Plan charges to the Golf Course be reallocated within the Community Services Department so as to not unfairly impact other General Fund activities. The ERA report indicates potential savings of $250,000 to $300,000 to the City should the City pursue private Golf Course maintenance. Staff will continue to monitor the increasing expenses to employee benefits currently at 50 percent of salary and determine if maintaining in-house operations is more economically or operationally efficient versus contracting out services. Staff will work with the labor union to ensure that, ultimately, the best services are provided to the community. Staff will continue to monitor ongoing revenue and expenditures to ensure that the Golf Course operation is a viable operation for the community.

The ERA report also points out the need for strategic capital investment in the Golf Course that includes rebuilding of selective greens and bunkers and improved golf cart storage to increase the number of carts in order to attract more and larger tournament play. The actual resource impact is to be determined with further analysis; however, the goal will be cost neutral capital improvement, as outlined in the study. That is, improvements which are economically justified by increased net operating income stemming from the improvements.

As mentioned above staff recommends that the Golf Course study be forwarded to the Finance Committee to work through the alternatives available to ensure ongoing success of the Golf Course operation and to return to Council with a feasible plan on how to proceed.

**ENVIRONMENTAL REVIEW**

No environmental review is needed at this time. However, should a Golf Course capital improvement project be considered at a future date all appropriate environmental review and consideration will take place prior to approval.

**ATTACHMENTS**

Attachment A: Economics Research Associates – Operational Analysis of the City of Palo Alto Golf Course

Attachment B: Executive Summary (Bullet Point Version)
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