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Title: ADOPT AN ORDINANCE GRANTING AMENDMENT NO. 1 TO AN OPTION TO LEASE AGREEMENT WITH SUNROAD HIE HOTEL PARTNERS, L.P. FOR A 66-YEAR LEASE TO DEVELOP AN UP TO 450-ROOM HOTEL ON HARBOR ISLAND TO EXTEND THE TERM OF THE OPTION

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Attachments: 1. 3. 2023-0079 Attachment A - Location Map, 2. 3. 2023-0079 Attachment B - Option to Lease Agreement, 3. 3. 2023-0079 Attachment C - Option Amendment No. 1, 4. 3. 2023-0079 Draft Ordinance

Date	Ver.	Action By	Action	Result
5/9/2023	1	Board of Port Commissioners	adopted	Pass

DATE: May 9, 2023

SUBJECT:

ADOPT AN ORDINANCE GRANTING AMENDMENT NO. 1 TO AN OPTION TO LEASE AGREEMENT WITH SUNROAD HIE HOTEL PARTNERS, L.P. FOR A 66-YEAR LEASE TO DEVELOP AN UP TO 450-ROOM HOTEL ON HARBOR ISLAND TO EXTEND THE TERM OF THE OPTION

EXECUTIVE SUMMARY:

Sunroad HIE Hotel Partners, L.P. (Sunroad) is proposing the development of the Sunroad Harbor Island East Hotel, which would involve demolition of the existing improvements within the project site, site preparation, and construction, including: grading, development, operation and maintenance of an up to 450-room hotel structure and associated amenities including a walk-up restaurant and bar area, swimming pool, jacuzzi spa, retail space, conference space, parking lot(s), waterfront promenade and landscaping (Project). The Project is located at the northeast corner of Harbor Island Drive and East Harbor Island Drive, consisting of two parcels totaling approximately 7.55 acres (Project Site).

On July 21, 2021, Sunroad entered into an Option to Lease Agreement (Option) with the San Diego Unified Port District (District) for the redevelopment of approximately 7.55 acres in East Harbor Island commonly referred to as the "Elbow Parcel" (Attachment A - Location Map). The Option, which includes and attaches a 66-year ground lease, (Lease), to be executed and effective after (1) Sunroad's satisfaction of all conditions precedent specified in the Option and (2) Sunroad's exercise of the Option. The Option had a term of two years which currently expires on May 31, 2023 and the conditions precedent are intended to ensure that upon exercise of the Option, Sunroad will be ready

to commence construction. Sunroad has been diligently working on its deliverables under the option agreement.

At the November 9, 2021 Board meeting, the Board adopted a resolution (BPC Resolution No. 2021-144) authorizing the issuance of an appealable Coastal Development Permit (CDP) for the Project, and the CDP (CDP-2021-07, on file in the Office of the District Clerk as Document No. 73453) was issued on December 7, 2021. Staff asked Sunroad whether they could feasibly incorporate lower cost accommodations onsite into the proposed hotel. Sunroad and District staff have been exploring an alternative which could result in another brand onsite, which would require changes to the design of the hotel.

In anticipation of a persistent challenge to obtaining hotel financing, coupled with the potential incorporation of lower cost accommodations onsite, Sunroad requested additional time to exercise its option. There is still additional work to be done to determine whether the onsite approach is feasible, including ongoing discussions with California Coastal Commission staff about the definition and enforcement of lower cost accommodations, as well as updated financial analysis to be conducted by District staff.

If the Board grants the option extension, staff will continue to work with Sunroad to incorporate lower cost accommodations onsite if feasible. If infeasible, Sunroad would still be allowed to pay in-lieu mitigation fees or develop (or contribute to the development of) lower cost accommodations elsewhere on tidelands. Under any of these scenarios, staff recommends the option extension to continue to advance the hotel project permitting and design while Sunroad waits for the hotel financing market to return. Staff believes that the extension is warranted and would allow Sunroad sufficient time to ensure all option conditions are met. Therefore, staff recommends extending the term of the Option by an additional two years, from May 31, 2023, to May 31, 2025 at no cost, and including two additional three-month extensions for a fee of \$100,000 per extension.

RECOMMENDATION:

Adopt an Ordinance granting Amendment No. 1 to an Option to Lease Agreement with Sunroad HIE Hotel Partners, L.P. for a 66-year lease to develop an up to 450-room hotel on Harbor Island to extend the term of the Option by two (2) years.

FISCAL IMPACT:

This agenda item has no fiscal impact.

COMPASS STRATEGIC GOALS:

This agenda item supports the following Strategic Goal(s).

- A vibrant waterfront destination where residents and visitors converge.
- A financially sustainable Port that drives job creation and regional economic vitality.

DISCUSSION:

The District and Sunroad entered into the Option on July 2, 2021. The Option includes conditions precedent that Sunroad is required to meet prior to exercising the Option and executing the Lease

(Attachment B - Option to Lease Agreement). These conditions, such as obtaining all necessary permits to construct the Project, providing proof of requisite debt and equity, and submission of hotel franchise and management agreements for District approval, are set forth in Section 4 of the Option and are in place to reasonably ensure that Sunroad is ready to commence construction upon exercise of the Option (and corresponding execution of the Lease). The Option has an initial term of two years expiring on May 31, 2023, and allows for two, three-month extensions (for a total of six months), which would be subject to the Executive Director's sole and absolute discretion and require payment of \$100,000 by Sunroad for each three-month extension.

Below is a summary of the conditions precedent set forth in the Option:

- A. Submittal of working drawings (due nine months prior to Option expiration);
- B. Proof of irrevocable commitment of project equity financing (due two months prior to Option expiration);
- C. Proof of irrevocable commitment of project debt financing (due two months prior to Option expiration);
- D. Submittal of development permits (due two months prior to Option expiration);
- E. Hotel franchise and management agreements (due four months prior to Option expiration and require Board approval);
- F. Submittal of completion guaranty (due one month prior to Option expiration);
- G. Submittal of an executed construction contract (due one month prior to Option expiration); and
- H. Conduct and submit an environmental site inspection (due two months prior to Option expiration).

Should all the conditions be met within the specified dates, Sunroad may exercise the Option and execute the Lease in the form attached to the Option.

The CDP contains additional conditions that Sunroad is required to satisfy before proceeding with its development, notably that Sunroad develop a certain number of rooms qualifying as lower cost accommodations, pay fees in lieu of developing lower cost accommodations, or a combination of developing lower cost accommodations and paying in-lieu fees. Staff asked Sunroad whether they could feasibly incorporate lower cost accommodations into the proposed hotel. Sunroad and District staff will need to conduct additional due diligence to determine whether this approach is ultimately feasible, including ongoing discussions with the California Coastal Commission regarding what qualifies as lower cost accommodations and a potential CDP amendment, as well as updated financial analysis to be conducted by District staff. If it is not feasible, then Sunroad has the in-lieu fee and offsite affordable accommodations available to use to continue to advance the hotel project.

Amendment No. 1 to the Option

Since the issuance of the CDP, Sunroad has been diligently working to satisfy the conditions in both the Option agreement and the CDP despite difficulties resulting from recent changes in the availability of financing for hospitality projects. In addition, and in consultation with District staff, Sunroad has been working on the Project's design, including considering the possibility of lower cost accommodations onsite. Staff believes an extension of the option term is warranted in light of these hurdles and in order to allow sufficient time to finalize Project design and satisfy other relevant Option and CDP conditions to better ensure the delivery of a successful hotel project. Therefore, staff recommends amending the Option to extend the term for an additional two years to May 31, 2025 at no cost, and to include the two preexisting additional three-month extensions for a fee of \$100,000

per extension, subject to approval by the Executive Director in his sole and absolute discretion (Attachment C - Amendment No. 1 to the Option).

General Counsel's Comments:

The Office of the General Counsel has reviewed this agenda sheet and the attachments as presented to it and approves the same as to form and legality.

Environmental Review

The proposed Board action to adopt an ordinance granting amendment No.1 to an option to lease agreement with Sunroad HIE Hotel Partners, L.P. for a 66-year lease to develop a hotel on Harbor Island was adequately analyzed in the First Addendum to the FEIR for the Sunroad Harbor Island Hotel Project and East Harbor Island Subarea Port Master Plan Amendment (UPD#83356-EIR-783; SCH #2006021027, Clerk Document No. 61175) prepared and adopted by the District on April 13, 2021 (Resolution No. 2021-059). The proposed project is not a separate project for CEQA purposes but is a subsequent discretionary approval related to a previously approved project. (CEQA Guidelines § 15378(c); Van de Kamps Coalition v. Board of Trustees of Los Angeles Comm. College Dist. (2012) 206 Cal.App.4th 1036.) Additionally, pursuant to CEQA Guidelines Sections 15162 and 15163, and based on the review of the entire record, including without limitation, the First Addendum to the FEIR, the District finds and recommends that the proposed Board action does not require further environmental review as: 1) no substantial changes are proposed to the project and no substantial changes have occurred that require major revisions to the previous First Addendum to the FEIR due to the involvement of new significant environmental effects or an increase in severity of previously identified significant effects; and 2) no new information of substantial importance has come to light that (a) shows the project will have one or more significant effects not discussed in the previous First Addendum to the FEIR, (b) identifies significant impacts more severe than those analyzed in the previous First Addendum to the FEIR, (c) shows that mitigation measures or alternatives are now feasible that were identified as infeasible and those mitigation measures or alternatives would reduce significant impacts, or (d) shows mitigation measures or alternatives which are considerably different from those analyzed in the previous First Addendum to the FEIR would substantially reduce one or more significant effects on the environment. Because none of these factors have been triggered, pursuant to CEQA Guidelines §15162(b), the District has determined no further analysis or environmental documentation is necessary. Accordingly, the proposed Board action is merely a step in the furtherance of the original project for which environmental review was performed and no supplemental or subsequent CEQA has been triggered, and no further environmental review is required.

The proposed Board action complies with Section 87 (a)(2) of the Port Act which allows for all visitor-serving commercial and industrial uses and purposes, and the construction, reconstruction, repair, and maintenance of commercial and industrial buildings, plants, and facilities. The Port Act was enacted by the California Legislature and is consistent with the Public Trust Doctrine. Consequently, the proposed Board action is consistent with the Public Trust Doctrine.

The proposed Board action was covered in the Coastal Development Permit (CDP) for Sunroad Harbor Island East Hotel Project (CDP-2021-07 dated December 7, 2021; Clerk Document No. 73453) approved for issuance by the District on November 9, 2021 (Resolution No. 2021-144). The proposed Board action is consistent with the CDP. No additional action under the California Coastal

Act is required at this time.

Diversity, Equity, and Inclusion Program:

This agenda sheet has no direct DEI impact on District workforce or contract reporting at this time.

PREPARED BY:

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Real Estate

Attachments:

Attachment A: Location Map
Attachment B: Option to Lease Agreement
Attachment C: Amendment No. 1 to Option to Lease Agreement