

(R-96-1028)


RESOLUTION NUMBER R- 287195

ADOPTED ON APR 15 1996

BE IT RESOLVED, by the Council of The City of San Diego, that the City Manager be and he is hereby authorized to implement the proposed flat-rate rents for aviation leases at Montgomery Field, as described in City Manager Report No. 96-71, attached hereto and incorporated herein.

APPROVED: JOHN W. WITT, City Attorney

By



Harold O. Valderhaug
Chief Deputy City Attorney

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The City of San Diego

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4-15-96

MANAGER'S REPORT

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CITY OF SAN DIEGO
COMMUNICATIONS SECTION

DATE ISSUED: April 10, 1996 **REPORT NO.** 96-71

ATTENTION: City Council Agenda of April 15, 1996

SUBJECT: Aviation Flat-Rate Rents, Montgomery Field

REFERENCE: CMR 93-124 dated April 26, 1993
Council Policy 700.15, (06/26/95)

SUMMARY

Issue: - Should the City Council approve the flat-rate rents being proposed for aviation leases at Montgomery Field?

Manager's Recommendation: - Approve the flat-rate rents being proposed for aviation leases at Montgomery Field for implementation by the City Manager.

Other Recommendations: - (1) The Airport Advisory Committee recommended approval of the proposed rents at its meeting of 12/27/95; (2) F.B.O. Resource Group determined the proposed rents are both reasonable and competitive, based on the competition; (3) The Real Estate Advisory Committee reviewed the proposed rents and did not recommend its adoption. The reason for this position is that should the Airports be privatized the rents could impact the Contractor's ability to generate revenue.

Fiscal Impact: - There will be a slight increase in revenue as new leases are executed at the new rents. The new rents are expected to attract new development to the airport during the next three years, resulting in a \$200,000 minimum annual increase in revenue.

BACKGROUND

In 1993, Council authorized City to convert its aviation leases from percentage rent basis to flat-rate. At that time, a flat-rate rent amount was approved for Brown Field and implemented. City is hereby submitting a range of flat-rate rents for Montgomery Field for Council approval.

Council adopted Policy 700-15 on June 26, 1995, in part, to assure the continued success of the City's aviation tenants. The proposed rents are in response to this policy that directs the City to "provide conditions where aviation service businesses can earn a reasonable profit".

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DISCUSSION

General aviation has been a depressed market for several years. Aircraft manufacturing peaked in the late 1970's, then came to a halt when a \$30 million dollar product liability suit drove insurance rates up, which crippled the industry. Luxury tax and the declining economy have also negatively affected the aviation industry. Tenants previously involved primarily in aircraft sales were forced to restructure their businesses and develop other sources of revenue. The aircraft base is declining as older aircraft leaving the market are not replaced, which consequently diminishes the market share for our aviation tenants. On a more positive outlook, sale of new aircraft seems to be making a slow recovery. According to the 11/95 issue of *In Flight USA* "General aviation aircraft shipments and billings for the first three quarters of 1995 continue to reflect a positive recovery for the industry..Units shipped were 714, up 16% for the year-to-date." Many of these sales are outside the country.

It can be difficult for new aviation businesses to succeed in this market, because they are often burdened with debt service and they do not have the benefit of an established clientele. Fortunately, the aviation tenants at Montgomery Field have the experience and established clientele to survive the current market. It is in the City's best interest, therefore, to retain these lessees whenever possible.

Method of Establishing Rents at Local Airports: *Rents at County Airports and Brown Field have been set either by policy or through arbitration, thus creating an artificial market.* Historically, the policy based methodology, based on a comparison of rental rates charged at other airports, has been commonly used in the industry, as mentioned in the 1994 appraisal, discussed below. This methodology has been widely used because there has not been sufficient data on aviation land sales or transfers to use for capitalized rent indicators. If there were, the rents could be based on a percentage of the land value.

In August 1994, the City hired an independent real estate appraiser to establish the aviation land rent at Montgomery Field. The appraisal opined that the market rent is between \$13,000 - \$15,000 per acre per year for the land, plus building rent. The appraised rent amount is approximately double what the City is currently receiving from its aviation leases at Montgomery. The City concluded after reviewing the appraisal that the appraiser may have focused too much on airports outside the area rather than on local airports. San Diego County and City airports share the same market and compete directly with each other for business and for tenants.

The City attempted to charge the appraised rent; however, the aviation tenants that had previously expressed interest in renewing their leases or developing land on the airport withdrew their interest, stating the appraised rent was more than their businesses

could financially support. City reviewed its last audits on the aviation businesses, as well as financial statements of tenants wishing to execute renewal leases, and that information essentially substantiated the tenants' claim.

Several factors were considered by staff when comparing the airports in preparing the range of rents: previous appraisals, length of runways, location, number of flight operations and based aircraft, existing infrastructure and improvements, growth potential, City aviation lease audits and fuel sales reports for the last five years on City airports, miscellaneous publications on current market data, and aviation business trends. Staff's survey revealed a huge discrepancy between the appraised rent and the actual rents being charged at local airports, so the City hired F.B.O Resource Group, Inc., a consultant specializing in appraising aviation property, to review the appraisal and the City's proposed rents.

F.B.O. Resource Group Inc.'s Findings:

City instructed the consultant to review the appraisal and the proposed rents, along with pertinent information on the surveyed airports, to determine if the flat-rate rents being proposed by City are reasonable and competitive, based on the local aviation market.

FBO Resource, Inc. noted that the previous appraiser's approach was not one typically used by industry appraisers, which resulted in the appraiser making, in their opinion, some inaccurate assumptions that influenced the outcome of the 1994 appraisal. The Consultant also determined the flat-rate rents being proposed by City are both reasonable and competitive, based on the local aviation market. The Consultant suggested further review of sites on a case by case basis. The City Manager will do this by exercising discretion in applying the range of rents, based on the amenities of each site and the proposed use.

CURRENT RENTS CHARGED AT LOCAL AIRPORTS, AS SURVEYED

<u>San Diego County Airports</u>	<u>Annual Flat-Rent/Acre Aviation</u>
McClellan Palomar Airport:	\$11,280 per acre
Gillespie Airport	\$4,200 per acre
Ramona & Borrego Airports	\$2,500 per acre
<u>City of San Diego</u>	
Brown Field Airport	\$3,800 per acre
<u>Proposed New Rent:</u>	
Montgomery Field (Developed & Undeveloped)	\$6,000-\$7,500 per acre

Note: The County stated it does not differentiate between developed or undeveloped land when applying the above rate. The rent for Brown Field is on developed sites. The other general aviation airports are not shown above, because the airports are not comparable to Montgomery Field.

Comparison of Local Airports: (See Exhibit "A") The focus of the survey was on Montgomery Field and the three more comparable airports in the area: Palomar, Brown Field, and Gillespie. The major difference separating Palomar and Brown Field from Gillespie and Montgomery Field is the length of the runways. Both Brown Field and Palomar Airports have longer runways for serving larger aircraft, thus creating the potential of generating higher revenues from fuel sales, aircraft sales, maintenance etc. This explains the higher rent at Palomar. Brown Field's rents are at the lowest of the four airports, because of its remote location and its condition.

Montgomery and Gillespie are similar in size and length of their runways; however, Montgomery has by far the best location of the four airports, because of its close proximity to major freeways and downtown. This location advantage will allow the City to charge higher rents than those charged by the County at Gillespie Field.

Because the rents have been policy based, staff did not find a measurable correlation between the individual airports characteristic advantages or disadvantages and the rents charged at those airports.

Implementation Of The New Rents: Rents between \$6,000 and \$7,500 will be charged for leases between three and fifteen acres. A rent of \$6,000 per acre will be charged on undeveloped parcels, sites under three acres, and sites over fifteen acres (for economic reasons), because: 1) Undeveloped sites require additional investment from the lessee; 2) sites under three acres are below the minimum size to allow effective utilization of the property for aviation use; 3) typically in the market, lease rent is reduced with the larger sites, plus these larger aviation businesses provide the majority of the airport's aircraft storage space. Although a very necessary airport service, aircraft tiedowns do not provide the highest return to the tenant. To encourage these larger aviation businesses to provide this essential service, the City is willing to offer the lower rent per acre.

Periodic Adjustments in the Rental Rates: The City Manager shall adjust the proposed market rents annually by increases in the CPI Index and also by increases indicated appropriate as a result of staffs annual rent surveys of local airports. Long-term leases will also contain periodic reviews of rental rates by appraisal and/or survey.

Additional Rents for Utilities and City-Owned Buildings: The amount

of the proposed flat-rents does not include utilities or building rents. Most of the buildings on the aviation sites are owned by the tenants and ownership is transferred to City at some future date.

The City leases a few old hangars, which are in short-term leases and Building 127 (frame/stucco). These buildings are in poor to fair condition and the initial rents are established by a staff rent survey of comparable buildings at local airports. These rents are periodically adjusted in accordance with the terms of the leases.

CONCLUSION

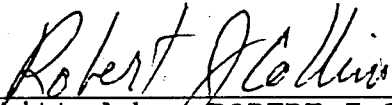
By approving the proposed rents, Council will allow the City Manager to gradually convert its leases to a flat-rate rent at Montgomery Field, thus creating an environment that allows the aviation tenants to earn a reasonable profit, in accordance with Council's direction on April 26, 1993 and per Council Policy 700-15. By establishing rents at the airport, staff will be able to negotiate renewal leases and expeditiously issue RFP's on vacant aviation parcels, bringing new business and revenues to the airport.

ALTERNATIVES

1. Do not approve the proposed flat-rate rents for Montgomery Field.
2. Approve some other flat-rate rents for aviation leases at Montgomery Field.

Respectfully submitted,


APPROVED: GEORGE I. LOVELAND
Deputy City Manager


Submitted by: ROBERT J. COLLINS,
Real Estate Assets Manager
(236-6144)

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EXHIBIT 'A', COMPARISON OF LOCAL GENERAL AVIATION AIRPORTS

	Montgomery Field Airport	Brown Field Airport	Ramona Airport	Gillespie Airport	Palomar Airport
Aircraft Operations	229,953	125,835	135,734	187,623	204,191
Runway	*3,400'	8,000'	4,000'	*4,040'	4,700'
Acres	546	900	396	743	439
Based Aircraft	589	200	210	858	469
Ground Rent Aviation	\$6,000-\$7,500 ac/yr	\$3,800 ac/yr	\$2,400 ac/yr	\$4,200 ac./yr	\$11,280 ac/yr

*Usable runway length after deducting displaced thresholds.
 This information was provided by staff at City and County airports.