

DATE ISSUED: November 4, 2009

ATTENTION: Honorable Chair and Members of the Redevelopment Agency
Docket of November 10, 2009

ORIGINATING DEPT.: Centre City Development Corporation

SUBJECT: Gaslamp Renaissance Hotel (block bounded by J Street and Fifth,
Sixth, and Island avenues) – Notice of Default in Accordance with
Disposition and Development Agreement between the
Redevelopment Agency of the City of San Diego and GRH, LLC –
Gaslamp Quarter Sub Area of the Centre City Redevelopment
Project

COUNCIL DISTRICT: 2

REFERENCE: None

STAFF CONTACT: Eli Sanchez, Senior Project Manager, 619-533-7121

REQUESTED ACTION: That the Redevelopment Agency of the City of San Diego (“Agency”) issue a notice of default to GRH, LLC (“Developer”) and HH Gaslamp, LLC (“Lessee”) in accordance with the Disposition and Development Agreement, as amended by that certain First Implementation Agreement to the Disposition and Development Agreement and that certain Second Implementation Agreement to the Disposition and Development Agreement (collectively the “DDA”) between the Developer and the Agency for the development and construction of a 365-room, full-service Marriott Renaissance Hotel (“Hotel”) located on the southwest corner of the block bounded by Fifth, Sixth and Island avenues and J street (“Site”) in the Gaslamp Quarter Sub Area.

STAFF RECOMMENDATION: That the Agency issue a notice of default to the Developer and Lessee in accordance with the DDA.

SUMMARY: The DDA was entered into on April 12, 2004, and provided for acquisition by the Agency, utilizing Developer’s funds, of an approximately 5,000-square-foot parcel (“Acquisition Parcel”) adjacent to the 35,000-square-foot site controlled by the Developer (“Developer Parcel”); the conveyance of the Acquisition Parcel to the Developer; and the timely redevelopment of the entire 40,000-square-foot Site (Attachment A) by the Developer in accordance with the DDA and Agency-approved plans. The Schedule of Performance was revised by the First Implementation Agreement of the DDA, dated April 26, 2006.

The Second Implementation Agreement, dated February 26, 2008, further extended the Schedule of Performance and approved amendments which provided for (i) an alternative means of conveyance of the Acquisition Parcel to the Developer from the Agency; (ii) a third-party ground lease ("Ground Lease") that provided for the partial delegation of certain DDA duties to HH Gaslamp, LLC ("Lessee"); and (iii) the express assumption of certain obligations of the Developer under the DDA by Lessee pursuant to that certain Delegation Agreement (without releasing Developer from all of its obligations under the DDA) consented to by the Agency. Pursuant to the terms and conditions of the Second Implementation Agreement, the Agency has conveyed the Acquisition Parcel to the Developer pursuant to that certain Grant Deed recorded on March 26, 2008 as Document No. 2008-0160297 in the Official Records of the Recorders Office for San Diego County (the "Grant Deed"). Although the Developer and Lessee were obligated to commence grading and excavation of the Site by January 12, 2009, construction has not commenced. The Developer and Lessee are now in default under the DDA.

Due to the challenging market conditions in the lodging industry, the Developer and Lessee requested an extension of the Schedule of Performance in the form of a Third Implementation Agreement (TIA). The purpose of the proposed TIA included amending the terms of the DDA to accomplish the following objectives:

1. Amend the Second Amended Schedule of Performance (DDA Attachment No. 3) to revise certain dates for performance of obligations under the DDA.
2. Amend the Scope of Development (DDA Attachment No. 4) to reflect the revised scope of the project.
3. Amend the DDA to reflect additional obligations of Developer relating to the delay in the development and construction of the improvements on the Site.

On July 22, 2009, the Centre City Development Corporation ("Corporation") considered the essential terms and conditions for a TIA and directed staff to proceed to the Agency with a recommendation to approve a TIA in accordance with the essential terms and conditions proposed at that meeting. After reaching an agreement with Corporation staff on the terms of the TIA, the Developer and Lessee failed to negotiate agreeable terms and conditions under which each party would proceed to implement the TIA under the Ground Lease and Delegation Agreement between the Developer and Lessee. Without the agreement by the Developer and Lessee to enter into the TIA to accomplish the objectives set forth in the paragraph above, the Corporation recommends that the Agency issue a notice of default.

FISCAL CONSIDERATIONS: The Developer has advanced funds in the amount of \$10,165,000 ("Developer Funds") for purchase of the Acquisition Parcel. The Agency retains approximately \$2.6 million in the Cash Security account to secure the Developer's obligations per the DDA.

CENTRE CITY DEVELOPMENT CORPORATION RECOMMENDATION: On July 22, 2009, the Corporation directed staff to proceed with negotiations for a TIA and recommended approval of a TIA in accordance with the essential terms and conditions proposed at the July 22

Corporation Board meeting. In the alternative, the Corporation directed staff to proceed to the Agency with a recommendation to issue a notice of default if the negotiations did not result in the execution of a TIA by the Developer and Lessee.

COMMUNITY PARTICIPATION AND PUBLIC OUTREACH EFFORTS: None.

DEVELOPMENT TEAM

ROLE	FIRM/CONTACT	OWNERSHIP
Developer	GRH, LLC, a California Limited Liability Company/Ramin Samimi	Ramin Samimi, Managing Member
Lessee	Hansji Hotels Gaslamp, LLC/Sajan Hansji	Privately owned
Architect	Awbrey, Cook, McGill Architects/ Tom Awbrey, Principal	Privately owned

BACKGROUND

The proposed construction of a high-density hotel project on this Site would have advanced the following visions and goals, guiding principles and strategies of the Centre City Community Plan and objectives of the Centre City Redevelopment Project by:

- Eliminating blight through the demolition and development of underutilized properties;
- Developing a strong financial/commercial core surrounded by mixed-use neighborhoods;
- Promoting the growth and vitality of Centre City as the primary business, educational, cultural and entertainment magnet;
- Providing property tax increment and Transient Occupancy Tax funding for the Ballpark and related infrastructure improvements through the addition of new hotel rooms;
- Downtown becoming a nucleus of economic activity and bolstering its position as the regional economic and employment center by ensuring availability of employment land and development of regional destinations;
- Maintaining Horton Plaza/Gaslamp Quarter as an entertainment and shopping district, with a broad mix of uses, high activity, and wide ranging appeal; and
- Ensuring an overall balance of uses that furthers downtown's role as the premier regional population, commercial, civic, cultural and visitor center.

The Agency, Developer and Owner of the Acquisition Parcel ("Owner") participated in a global settlement conference on December 19, 2007 that resulted in the settlement of the eminent domain litigation. The settlement between the Agency and the Owner generally provided for the execution of settlement documents between the Owner and Agency approved by Agency legal counsel which, among other things, provided that the Agency pay the Owner a total of \$7,800,000 from the funds deposited by the Agency with the court (less amounts already disbursed and other legally required deductions) for the purchase of the Acquisition Parcel, and provided that all pending litigation between the Agency and Owner be settled.

The Developer has achieved approval of the 100 percent Design Development Drawings, has completed a Phase II Environmental Site Assessment, and prepared a Property Mitigation Plan. In addition, the Developer has submitted to the City of San Diego's Building Department revised excavation, shoring and grading plans to include a third level of parking. These plans are presently in the third round of review and are in the process of clearing plan check. The Second Implementation Agreement provided for amending the Scope of Development to increase the number of room keys from approximately 334 to approximately 365; amending the Method of Financing; amending the provision for an alternative means of conveyance of the Acquisition Parcel to the Developer from the Agency; and approving the Ground Lease and the partial delegation of certain DDA duties to the Lessee under a Delegation Agreement.

The Agency holds a First Deed of Trust on the Acquisition Parcel and a Cash Security in the amount of approximately \$2.6 million. The purpose of the First Deed of Trust and Cash Security is to secure performance of the Developer pursuant to the DDA. In the event Developer or Lessee fails to timely cure a default of its obligations under the DDA as amended, the Agency may retain the entire Cash Security (with interest, if any) as Agency funds and it shall be deemed to be minimum damages.

DISCUSSION

Under the DDA, as revised by the First and Second Implementation Agreements, the Developer was to commence grading and excavation by January 12, 2009, and complete construction by April 22, 2011. The Developer and Lessee are now in default under the DDA, as amended, as follows:

1. Developer and Lessee failed to prepare and submit 80 Percent Construction Drawings to the Agency by November 17, 2008.
2. Developer and Lessee failed to obtain grading, excavation and shoring permits by December 1, 2008.
3. Developer and Lessee failed to commence grading and excavation by January 12, 2009.
4. As set forth in the attached Notice of Default.

The Lessee acknowledges suspension of all predevelopment work, based on the current condition of the economy, market uncertainty and deterioration of the overall lodging industry. The Developer and Lessee find it difficult to secure financing given the unprecedented decline in the economy and capital markets. Due to the extremely challenging market conditions in the lodging industry, the Developer and Lessee requested an extension of the Schedule of the Performance in the form of a TIA.

The purpose of the proposed TIA included amending the terms of the DDA to accomplish the following objectives:

1. Amend the Second Amended Schedule of Performance (DDA Attachment No. 3) to revise certain dates for performance of obligations under the DDA.

2. Amend the Scope of Development (DDA Attachment No. 4) to reflect the revised scope of the project.
3. Amend the DDA to reflect additional obligations of Developer relating to the delay in the development and construction of the improvements on the Site.

On July 22, 2009, the Corporation considered the essential terms and conditions of a TIA and directed staff to proceed to the Agency with a recommendation to approve a TIA in accordance with the essential terms and conditions proposed at that meeting. The Corporation also directed that if negotiations for the TIA did not result in an agreement by the Developer and Lessee to enter into the TIA, that staff proceed to the Agency with a Corporation recommendation for the Agency to issue a notice of default in accordance with DDA.

The Developer and Lessee had agreed in concept to the terms and conditions for a draft TIA as negotiated between the Agency (as represented by the Corporation), Developer and Lessee in accordance with the essential terms and conditions presented at the July 22 Corporation meeting (Attachment B). Below is a summary of the essential terms of the TIA:

1. Extend the Schedule of Performance to provide for the start of grading and excavation from January 12, 2009 to December 28, 2012.
2. Developer to pay \$100,000 per year as consideration for the extension of the Schedule of Performance. Payments to be withdrawn from the Cash Security by the Agency on a quarterly basis beginning December 30, 2009 for the quarter commencing October 1, 2009 and shall continue every quarter until Agency receives 80% construction drawings and specifications.
3. Developer to make temporary repair of including, but not limited to, sidewalks, curbs and gutters along J Street, Fifth and Sixth avenues.

However, the Developer and Lessee have failed to negotiate agreeable terms and conditions under which each party would proceed to implement the TIA under the Ground Lease and Delegation Agreement. Without the agreement by the Developer and Lessee to enter into the TIA, the Corporation recommends that the Agency issue (i) a notice of default and 30-day opportunity to cure all defaults under the DDA in the form attached as Attachment C; and (ii) other necessary notices of default under documents entered into in connection with the Agreement, including, without limitation, related to exercising the right of reverter under the Grant Deed.

The Agency holds a First Deed of Trust on the Acquisition Parcel and a Cash Security in the amount of approximately \$2.6 million. The purpose of the First Deed of Trust and Cash Security is to secure performance of the Developer pursuant to the DDA. In the event of failure to timely cure any default, the Agency may retain the entire Cash Security (with interest, if any) as minimum damages.

By letter dated September 30, 2009, Cynthia Eldred, counsel for the Developer, sent a letter to Murray O. Kane, Agency Special Counsel, addressing, among other things, Developer and Lessee's inability to negotiate and agree to the terms of the TIA, Lessee's unwillingness to move forward with the project and Developer's desire to enter into the TIA to complete the project.

By letter dated September 30, 2009, Murray O. Kane, Agency Special Counsel, sent a letter to Cynthia Eldred, Developer's counsel, reaffirming the Agency's right to look to both Developer and Lessee to perform all obligations of Developer under the DDA, and the Agency's right to pursue all available remedies thereunder.

Scope of the Project – The proposed Hotel is an approximately 365-room, 12-story Marriott Renaissance hotel, approximately 240,684 square feet above grade, consisting of a first class, full-service hotel with a 5,000-square-foot ballroom, 5,328 square feet of meeting rooms, 3,252 square feet of prefunction space, three levels of subterranean parking for 256 vehicles, and 12,062 square feet of retail/commercial uses, located on a 40,000-square-foot parcel on the block bounded by J Street and Fifth, Sixth and Island avenues in the Gaslamp Quarter. The total height of the development will not exceed 125 feet and a Floor Area Ratio (FAR) of 5.99.

Project Budget and Financing – The Developer is responsible for all costs and expenses associated with the assembly of the Site and the development and construction of the improvements on the Site.

Disposition of Property – In accordance with the DDA and the global settlement agreement to settle the Mesdaq eminent domain litigation, the Agency conveyed the Acquisition Parcel to the Developer. The Agency holds a First Deed of Trust on the Acquisition Parcel to secure performance of the Developer pursuant to the DDA.

Participation by Agency – The Agency holds a First Trust Deed and Cash Security in the amount of approximately \$2.6 million and may withdraw funds from the Cash Security to mitigate damages to the Agency resulting from the delay in commencement of construction and the subsequent opening of the Hotel.

Ground Lease – In accordance with the DDA, the Developer has entered into the Ground Lease with HH Gaslamp, LLC, a California limited liability company, to construct and operate the Hotel under a management agreement with Marriott. The Lessee would build the Hotel in accordance with the DDA and the approved Development/Site Permit No. 41-0546. The Lessee does not have an option to purchase the fee simple interest in the property. The Ground Lease would not be subordinated to any loans on the property made by the Lessee. The Ground Lease is subordinate to the Agency's right-of-reverter contained in the Grant Deed until the issuance by the Agency of a Release of Construction Covenants pursuant to that certain Subordination

Agreement between Developer and Lessee.

The Developer and Lessee have entered into a Delegation Agreement in form and substance approved by the Agency, wherein the Lessee assumed certain obligations of the Developer under the DDA. The Delegation Agreement does not release the Developer from its obligations under the DDA. The Developer has issued a notice of default under the Ground Lease and has demanded that the Lessee cure all outstanding defaults within 30 days.

Environmental Impact – This activity is not a “project” under the definition set forth in CEQA Guidelines Section 15378. Therefore, pursuant to CEQA Guidelines Section 15060(c) (3), the activity is not subject to CEQA.

CONCLUSION

The Developer and Lessee are in default of the DDA as amended by the Second Implementation Agreement and the Grant Deed and have failed to agree to enter into a TIA to extend the Schedule of Performance and amend the DDA to reflect additional obligations of Developer relating to the delay in the development and construction of the improvements on the Site. The Corporation recommends that the Agency issue a notice of default in accordance with the DDA, and other necessary notices of default under documents entered into in connection with the DDA, including, without limitation, related to exercising the right of reverter under the Grant Deed.

Respectfully submitted,

Concurred by:



Eli Sanchez
Senior Project Manager



Frank J. Alessi
Executive Vice President & Chief
Financial Officer

Attachments: A – Site Map
B – Draft Third Implementation Agreement
C – Form of Notice of Default