

**CITY OF SANTA BARBARA WATERFRONT DEPARTMENT**

**MEMORANDUM**

**Date:** February 18, 2010  
**To:** Harbor Commission  
**From:** John N. Bridley, Waterfront Director  
**Subject:** Lease Amendment with Chuck's Waterfront Grill

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**RECOMMENDATION:**

That Harbor Commission consider and recommend to City Council approval of a lease amendment with Richones, Inc. doing business as Chuck's Waterfront Grill, 113 Harbor Way, in order to amend the "Reimbursement for Improvements" clause common to restaurant leases for tenant capital improvements.

**BACKGROUND:**

The lease agreement between the City and Chuck's Waterfront Grill (Chuck's) was executed on February 28, 1997. Chuck's leases 4,888 square feet of interior space and 2,617 of outdoor patio space on the first and second floors of the Waterfront Center Building. The base rent is currently \$206,360 per year (average of \$17,197 per month), or 10% of gross sales, whichever is greater. The percentage rent escalates to 11% of gross sales if the tenant exceeds \$3 million in gross sales in a calendar year, which occurred in 2008. The base rent is subject to an annual cost of living adjustment based on the Consumer Price Index (CPI). The tenant also reimburses the City for its proportional share of Common Area Maintenance (CAM) expenses for the Waterfront Center Building; Chuck's proportional share is currently \$4,466 per month. The lease was originally a five-year lease with seven five-year options, for a total possible term of 40 years (same term as the Maritime Museum). The initial lease term expired on February 29, 2004, and the first option to extend expired on February 28, 2009. The tenant has 30 years remaining on the lease.

**DISCUSSION:**

For several years, Chuck's owners Larry Stone and Steve Hyslop have expressed interest in changing the color of the exterior of the Waterfront Center Building to something they feel would be more inviting than the current white color. Additionally, the ground floor patio is exposed to wind and the elements and does not have glass wind screening common to other ocean-front restaurants such as Breakwater Restaurant, Shoreline Beach Café, the Boathouse, and Beachside Bar-Café at Goleta Beach.

The Waterfront Center Building is designated as a historical landmark by the State Historic Landmarks Office (SHPO) and any changes to the exterior of the building are subject to review and approval of the City's Historic Landmarks Committee (HLC). Since 2007, Chuck's has been engaged in the HLC approval process to restore the exterior building to its original ochre color, add a glass windscreen around the ground floor patio, add radiant or forced-air heating to the patio, and construct a canvas sail-like awning over the patio area (Attachment 2). Chuck's architect David van Hoy presented the tenant improvement plan to the Harbor Commission on November 16, 2006. Chuck's now has approved plans and permits and is ready to proceed with the patio improvements. Chuck's solicited proposals from several contractors and the cost of the tenant improvement is estimated to be approximately \$300,000. The Department has budgeted an additional \$75,000 for painting the building and trim; the cost to the Department will be reimbursed from the CAM charges paid by the Maritime Museum and Chuck's.

Chuck's owners believe they can increase lunch and dinner service on the ground floor patio significantly with the proposed improvements. Certified Public Accountant Michael Schmitchen submitted a proforma indicating that Chuck's sales are expected to increase by 18% in the year following the completion of the improvements and 3% per year thereafter. The increase in sales would result in a corresponding increase in percentage rent payments to the Department of approximately \$50,000 annually. Within approximately three years, the Department's contribution to the project would be paid for by the increase in gross sales and percentage rent paid.

### **Reimbursement for tenant Improvements**

In December 1997, the Harbor Commission reviewed and approved what is referred to as a "Reimbursement for Improvements" lease provision (Attachment 1). The Reimbursement for Improvements provision allows eligible tenants to apply for an offset to their percentage rent for certain infrastructure improvements that are approved in advance by the Department (the tenant is still responsible for paying its full base rent obligation). Tenants that have the Reimbursement for Improvements clause in their lease include Brophy Brothers, Char West, Harbor Restaurant, Minnow Café, Shoreline Beach Café, SB Shellfish Company, Sea Landing and SB Sailing Center. The clause is intended to encourage tenants to invest in the infrastructure of the property, which benefits the tenant and the City, and the property ultimately reverts to City ownership at lease expiration. For example, Brophy Brothers and the Harbor Restaurant completed major kitchen and plumbing upgrades to their leased properties under the rent credit incentive program. Shoreline Beach Café added its awning and forced-air heating to its outdoor patio and received rent credits under the program; the tenant's sales and percentage rent payments increased following the improvement.

Chuck's intends to use the Reimbursement for Improvements incentive program to make the patio improvements to the Waterfront Center building; however, the current formula (10% of annual rent paid) amounts to a total possible rent credit of \$27,000-\$30,000. Due to the high cost of the patio improvements, estimated at \$300,000,

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Chuck's asked for a one-time increase to the Reimbursement for Improvements clause of \$150,000 for the patio project. The tenant will continue to make base rent payments (currently \$206,000/year) and the \$150,000 rent credit will be offset against Chuck's monthly percentage rent obligation until the \$150,000 is absorbed (approximately 1½ to 2 years). After calendar year 2010, the Reimbursement for Improvements clause will revert to the regular formula of 10% of actual rent paid.

A similar enhanced Reimbursement for Improvements provision was negotiated with the Harbor Restaurant when it expanded its patio and patio enclosure in 2002.

The basic business terms of the lease will remain unchanged. A copy of the proposed amendment is available for review at the Waterfront Department Administration office.

Attachments: 1. Harbor Commission Minutes December 18, 1997  
2. Site Plan  
3. VanHoy Project Proposal

Prepared by: Scott Riedman, Waterfront Business Manager