TORONTO

STAFF REPORT
ACTION REQUIRED

St. Lawrence Market (South) – New Lease Agreements

Date:	February 25, 2010
To:	Government Management Committee
From:	Chief Corporate Officer
Wards:	Ward 28 – Toronto Center-Rosedale
Reference Number:	P:\2010\Internal Services\RE\Gm10021re (AFS 11657)

SUMMARY

The purpose of this report is to obtain authority to enter into new lease agreements with sixty-five (65) commercial tenants (see “Appendix A”) in the St. Lawrence Market South building.

RECOMMENDATIONS

The Chief Corporate Officer recommends that:

1. City Council grant authority to enter into lease agreements (the "Agreements") between the City of Toronto, as landlord, and sixty-five (65) tenants, as outlined in “Appendix A,” in the building known municipally as 91, 93 and 95 Front Street East (St. Lawrence Market South) substantially on the terms and conditions as set out in “Appendix B” attached hereto and on such other terms and conditions as approved by the Chief Corporate Officer, or his or her designate, and in a form acceptable to the City Solicitor.

2. City Council authorize the Chief Corporate Officer to administer and manage the Agreements including the provision of any consents, approvals, notices and notices of termination provided that the Chief Corporate Officer may, at any time, refer consideration of such matters (including their content) to City Council for its determination and direction.

Financial Impact

The proposed Agreements, commencing retroactively on January 1, 2010, provide for a common rate structure and terms, as outlined in Appendix "B", and will result in the following revenue for the City:

	2010	2011	2012	2013	2014
Base Rent [1]	$2,090,894	$2,221,157	$2,229,481	$2,229,481	$2,229,481
Additional Rent [2]	$895,551	$895,551	$895,551	$895,551	$895,551
TOTAL	**$2,986,445**	**$3,116,709**	**$3,125,032**	**$3,125,032**	**$3,125,032**

[1] Includes semi-gross rent, storage rent and percentage rents
[2] Based on 2009 – actual costs will be passed through to the Tenants

With the new rates and after considering all revenues and expenses for the South Market, alongside capital repair requirements and the opportunity cost of City occupied space, the South Market operates close to a break-even position.

The Deputy City Manager and Chief Financial Officer has reviewed this report and agrees with the financial impact information.

DECISION HISTORY

St. Lawrence Market (South) has been operating as a food market and shopping venue for over one-hundred (100) years. The Market currently has sixty-seven (67) vendors selling a range of food products, including fruits and vegetables, fish, meats, grain, baked goods and diary products, and unique non-food items. The South Market draws wide support from customers across the Greater Toronto Area, as well as tourists.

Under Delegated Authority Form No. 99-048 dated March 9, 2009 and Delegated Authority Form No. 99-224 dated January 27, 2000, the Chief Administrative Officer authorized a five (5) year lease agreement with fifty-four (54) tenants, commencing on January 1, 1999 and ending on December 31, 2003.

Under Delegated Authority Form No. 2004-024 dated May 4, 2004, the Chief Administrative Officer authorized the extension of fifty-four (54) leases for an additional five (5) year term, commencing on January 1, 2004 and ending on December 31, 2008.

At its meeting on April 29 and 30, 2009, City Council authorized the extension of sixty-four (64) St. Lawrence Market (South) leases, on the same terms and conditions existing

at the time, for a one year term ending on December 31, 2009. The Council decision can be found through the following hyperlink:
http://www.toronto.ca/legdocs/mmis/2009/mm/bgrd/backgroundfile-20871.pdf

ISSUE BACKGROUND

The City has sixty-five (65) commercial tenants in St. Lawrence Market (South) whose leases expired on December 31, 2009 (there are two (2) additional Tenants with leases that expire at a later date). The current lease agreements were based on rates, terms and conditions established in the renewal agreement dated January 1, 2004. As such, updated Agreements are required to achieve current market rates and reflect updated lease terms generally required by the City.

COMMENTS

Rent Structure, Tenant Categories and Term

Under the current lease agreements, gross rents range from $41 per square foot to $106 per square foot. Additional rents (landlord expense recoveries) also fluctuate significantly, and are not sufficient to cover the actual expenses incurred by the City, resulting in negative net operating income for the South Market.

The proposed agreement recommends a standard rate structure based on comparable market data, along with standard terms and lease conditions. This allows City staff to administer the leases with greater consistency and efficiency, while achieving standard rates that reflect the value of South Market space and allow all landlord expenses to be recovered. A study of rental rates for individual tenants was conducted on behalf of the City by Cushman & Wakefield LePage. Market value was determined through an evaluation of local comparable market data and a review of other speciality markets.

Suitable rental rates were determined using a method known as Occupancy Cost to Store Gross Revenue (“GROC”). This method determines the ratio between gross operating costs charged by the Landlord vs. gross revenues generated by the Tenant, and uses industry benchmarks to measure the ability of a Tenant to absorb lease related occupancy costs (in relation to expected revenues). Using this approach and the recommendations provided by Cushman & Wakefield Lepage, rental rates were established by Tenant categories. The proposed Agreement is for a semi-gross rental rate of $46.00 per square foot of rentable area on the lower level. Those tenants located on the upper level (33 in total) will be charged a 15% premium (semi-gross rate of $52.90) on the semi-gross rate, reflecting their relative advantage over lower floor Tenants on customer accessibility, visibility and traffic.

City staff have agreed to help Tenants absorb the new rate structure by limiting increases in *gross* rents to 25% year-over-year, per Tenant (before percentage rents and storage rents). Twenty-five (25) Tenants are affected by increases over 25% in the first year, but all Tenants are projected to pay market rents by the third year of the term. Once all Tenants are at the full market rate, it will represent an average increase in total occupancy costs of 22% per tenant when compared to current/2009 rates.

Tenant categories 1-4 (as described in "Appendix B") were created to recognize the differences in demand and expected revenue potential for different product types. Category 1 stores typically attract higher demand and consumer volumes, which generate higher revenues than other categories. Other categories are expected to attract more moderate demand and consumer traffic, particularly Category 3 and 4, some of which do not fit with the typical brand/make-up of St. Lawrence Market Tenants. Considering the uncertainty associated with the latter categories, a risk premium has been established as a component of percentage rents.

Recommended terms vary from two (2) to five (5) years and have been negotiated taking into account Tenant's current performance, ability, product mix desirability and future potential. Recommended terms by Tenant are provided in "Appendix A." City staff have negotiated the terms and conditions as outlined in this report with the South Market Tenants and have reached a mutually acceptable agreement.

Financial Position

With the new rates, the City is projecting net operating income of $185,392 for the South Market in the first year of the term. This includes all revenues for the South St. Lawrence Market, including market cart rentals, parking income and ATM revenues, alongside all costs to operate the South Market. Net operating income is projected to grow to approximately $240,000 by the fifth year of the Agreement.

Costs to operate the South Market are substantial, partially due to the unique design and age of the building. There is over 111,458 square feet of building area, of which only 35% contributes to rentable sales area. This has substantial implications on common area and maintenance costs, particularly as it relates to custodial and operations work. The South Market is also a heritage building. Preserving the building and maintaining is heritage character presents additional costs that are beyond the scope of typical shopping venues. After considering projected annual capital costs, the City expects a net direct loss of approximately $289,000 per year (net operating income, after capital).

The City also occupies approximately 10,235 square feet of area in the building for the "Market Gallery." City staff estimate that 5,118 of this area is rentable space that could otherwise be leased at market rates. The opportunity cost of using this space for City purposes, under the new rate structure, is $270,742 per year. After considering all revenues and expenses for the South Market, alongside capital repair requirements and the opportunity cost of City occupied space, the South Market operates close to a break-even position.

Short-Term Lease Program and Business Incubator Program

In recognition of the current market climate and the unique nature of the Market, staff are proposing two new leasing programs for the South Market:

1.) The St. Lawrence Market Business Incubator Program is intended to assist *new* businesses in the Market. Businesses that qualify for the program will receive a 50% reduction in base rent, with slightly higher percentage rents (8%), on 1-3 year lease terms. The intention is to provide new businesses the opportunity to succeed in a new environment. There are no recommended vendors in this program at this time.

2.) To encourage underperforming operations to improve their business models, a Short Term Lease Program is also being proposed for Tenants performing below standards. Under this program, affected Tenants will be given specific performance criteria to achieve within specific timeframes, coupled with business consultations and support provided by City staff. Businesses that meet performance targets may qualify for lease extensions. Failure to meet expectations may result in termination of the Tenant's Agreement and provide an opportunity for new businesses to occupy the leased space. It is recommended that fourteen (14) current vendors be included in this program, as outlined in "Appendix A."

Staff consider the terms and conditions of the proposed agreement to be fair and reasonable, and at market rates.

CONTACT

Joe Casali
Director, Real Estate Services
Tel: (416) 392-7202
Fax: (416) 392-1880
jcasali@toronto.ca

SIGNATURE

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Bruce Bowes, P. Eng.
Chief Corporate Officer

ATTACHMENTS

Appendix "A" – Tenant Information
Appendix "B" – Major Terms and Conditions
Appendix "C" – Location Map