



## REGULAR MEETING

### OVERSIGHT BOARD FOR THE SUCCESSOR AGENCY TO THE CITY OF SOUTH SAN FRANCISCO REDEVELOPMENT AGENCY

P.O. Box 711 (City Hall, 400 Grand Avenue)  
South San Francisco, California 94083

CITY HALL  
LARGE CONFERENCE ROOM, TOP FLOOR  
400 GRAND AVENUE

TUESDAY, DECEMBER 11, 2012  
2:00 P.M.

#### PEOPLE OF SAN MATEO COUNTY

You are invited to offer your suggestions. In order that you may know our method of conducting Board business, we proceed as follows:

The regular meetings of the South San Francisco Oversight Board for the Successor Agency to the City of South San Francisco Redevelopment Agency are held on the second Tuesday of each month at 2:00 p.m. in the in the Large Conference Room, Top Floor at City Hall, 400 Grand Avenue, South San Francisco, California.

In accordance with California Government Code Section 54957.5, any writing or document that is a public record, relates to an open session agenda item, and is distributed less than 72 hours prior to a regular meeting will be made available for public inspection in the City Clerk's Office located at City Hall. If, however, the document or writing is not distributed until the regular meeting to which it relates, then the document or writing will be made available to the public at the location of the meeting, as listed on this agenda. The address of City Hall is 400 Grand Avenue, South San Francisco, California 94080.

In compliance with Americans with Disabilities Act, if you need special assistance to participate in this meeting, please contact the South San Francisco City Clerk's Office at (650) 877-8518. Notification 48 hours in advance of the meeting will enable the City to make reasonable arrangements to ensure accessibility to this meeting.

**Chairperson:**

Neil Cullen

**Selected by:**

Largest Special District of the type in H&R  
Code Section 34188

**Vice Chair:**

Denise Porterfield  
Deputy Superintendent, Fiscal and Operational Services  
San Mateo County Office of Education

**Selected by:**

San Mateo County Superintendent of Schools

**Board Members:**

Mark Addiego  
Councilmember, City of South San Francisco  
Alternate: Barry Nagel  
City Manager, City of South San Francisco

**Selected by:**

Mayor of the City of South San Francisco

Gerry Beaudin  
Principal Planner, City of South San Francisco

Mayor of the City of South San Francisco

Barbara Christensen  
Director of Community/Government Relations,  
San Mateo County Community College District

Chancellor of California Community College

Reyna Farrales  
Deputy County Manager, San Mateo County

San Mateo County Board of Supervisors

Paul Scannell

San Mateo County Board of Supervisors  
(Public Member)

**Counsel**

Michael Roush as alternate for Craig Labadie

**Advisory:**

Marty Van Duyn – Assistant City Manager, City of South San Francisco  
Jim Steele – Finance Director, City of South San Francisco  
Steve Mattas – City Attorney, City of South San Francisco  
Krista Martinelli – City Clerk, City of South San Francisco  
Armando Sanchez – Redevelopment Consultant, City of South San Francisco

**CALL TO ORDER**

**ROLL CALL**

**PLEDGE OF ALLEGIANCE**

**AGENDA REVIEW**

## PUBLIC COMMENTS

Comments from members of the public on items not on this meeting agenda. The Chair may set time limit for speakers. Since these topics are non-agenda items, the Board may briefly respond to statements made or questions posed as allowed by the Brown Act (Government Code Section 54954.2). However, the Board may refer items to staff for attention, or have a matter placed on a future agenda for a more comprehensive action report.

## MATTERS FOR CONSIDERATION

1. Motion to approve the Minutes of the Regular Meeting of November 13, 2012.
2. Discussion item on Proposition 1A implications of County Controller's methodology for allocating Redevelopment Property Tax Trust Fund (RPTTF) Proceeds.
3.
  - a) Discussion of the State of California Department of Finance (DOF) response to the Chairman of the Oversight Board's letter requesting guidance on unfunded pension and retirement health liabilities (unfunded liabilities) being an enforceable obligation of the Successor Agency (SA) of the South San Francisco Redevelopment Agency (RDA).
  - b) Possible Oversight Board (OB) direction to staff on developing a request to include unfunded liabilities on a subsequent Recognized Obligations Payment Schedule (ROPS).
4. Discussion and direction related to Reorganization of the Oversight Board.
5. Closed Session:  
Real Property Negotiations  
(Pursuant to Government Code Section 54956.8)  
Related to: 1 Chestnut Avenue  
Negotiating Parties: Oversight Board and Successor Agency for the former South San Francisco Redevelopment Agency and Red Cart Market Inc., dba Pet Club Stores.  
Agency Negotiator: Marty VanDuyn.  
Red Cart Market Inc., dba Pet Club Stores Negotiator: Vic Catanzaro.
6. Resolution approving the Lease between the South San Francisco Successor Agency and Pet Club for the property located at One Chestnut Avenue in South San Francisco.
7. Future Agenda Items.
  - a) Property Disposition Plan.

8. Closed Session:  
Conference with Legal Counsel - Existing Litigation  
(Pursuant to Government Code 54956.9(a))  
Metwally v. South San Francisco Successor Agency.

ADJOURNMENT



# REGULAR MEETING MINUTES

**DRAFT**

## OVERSIGHT BOARD FOR THE SUCCESSOR AGENCY TO THE CITY OF SOUTH SAN FRANCISCO REDEVELOPMENT AGENCY

P.O. Box 711 (City Hall, 400 Grand Avenue)  
South San Francisco, California 94083

CITY HALL  
LARGE CONFERENCE ROOM, TOP FLOOR  
400 GRAND AVENUE

TUESDAY, OCTOBER 13, 2012  
2:00 P.M.

### CALL TO ORDER

Time: 2:02 p.m.

### ROLL CALL

Present: Boardmembers Addiego, Beaudin,  
Christensen, Farrales and Scannell, Vice  
Chairperson Porterfield and Chairperson  
Cullen.

Absent: None.

### PLEDGE OF ALLEGIANCE

Led by Vice Chairperson Porterfield.

### AGENDA REVIEW

None.

### PUBLIC COMMENTS

Comments from members of the public on items not on this meeting agenda. The Chair may set time limit for speakers. Since these topics are non-agenda items, the Board may briefly respond to statements made or questions posed as allowed by the Brown Act (Government Code Section 54954.2). However, the Board may refer items to staff for attention, or have a matter placed on a future agenda for a more comprehensive action report.

None.

## MATTERS FOR CONSIDERATION

1. Motion to approve the respective Minutes of the Regular Meeting of October 9, 2012 and Special Meeting of October 19, 2012.

Motion – Boardmember Scannell/Second– Boardmember Addiego: to approve the Minutes of the Regular Meeting of October 9, 2012. Approved by the following voice vote: AYES: Boardmembers Addiego, Beaudin, Christensen and Scannell, Vice Chairperson Porterfield and Chairperson Cullen. NOES: None. ABSTAIN: Boardmember Farrales. ABSENT: None.

Motion – Boardmember Scannell/Second– Boardmember Addiego: to approve the Minutes of the Special Meeting of October 19, 2012. Approved by the following voice vote: AYES: Boardmembers Addiego, Beaudin, Christensen and Scannell, and Chairperson Cullen. NOES: None. ABSTAIN: Boardmember Farrales and Vice Chairperson Porterfield. ABSENT: None.

2. Discussion pertinent to scheduling a Special Meeting in January 2013 for approval of the Due Diligence Review (DDR)- Non-Housing Funds after such DDR is presented for Board review and public comment at the Regular Meeting of January 8, 2013.

Boardmembers tentatively scheduled a Special Meeting for January 15, 2013 at 2:00 p.m. for approval of the Due Diligence Review (DDR)- Non-Housing Funds after such DDR is presented for Board review and public comment at the Regular Meeting of January 8, 2013.

3. Authorize Oversight Board Chairman to send letter to the State of California Department of Finance (“DOF”) requesting guidance about unfunded pension and retiree health liabilities being enforceable obligations of the Successor Agency of a Redevelopment Agency.

Chairperson Cullen advised Boardmembers he had drafted the proposed letter seeking the DOF’s position on the enforceable obligation status of unfunded pension and retiree health liabilities associated with City employees who served the RDA in some capacity but were not technically employed by the RDA. He noted that recent legislation had addressed this issue with respect to terminations of RDA employees, but did not address the specific issue confronting the South San Francisco Successor Agency and Oversight Board. He suggested the taxing entities would benefit from an affirmative answer as to whether this is an enforceable obligation so that funding methodologies might be considered.

Boardmember Addiego requested that the Successor Agency and not the City be identified in the second paragraph of the letter. Boardmembers agreed.

In response to Boardmember Scannell’s question regarding the nexus between the City employee positions listed and RDA service, Counsel Labadie advised that Chairperson Cullen’s proposed letter only addressed the threshold legal question as to whether the Successor Agency would be entitled to reimbursement. If the DOF’s position is that such obligations are enforceable, then it would be up to the Oversight Board to make the factual determination as to which employee obligations/amounts to

include.

Boardmember Beaudin stated his preference for Option B in the memorandum which would involve the Oversight Board taking the up-front position that these are enforceable obligations as opposed to first requesting the opinion of DOF. He questioned whether other Oversight Boards had already taken this position.

Counsel Labadie advised some Oversight Boards had approved similar obligations subject to review by DOF. He noted that the Board would be spared calculations pertinent to the potential obligations if DOF's position was that such obligations were unenforceable.

Motion – Boardmember Scannell/Second– Boardmember Christensen: to authorize the Oversight Board Chairman to send a letter to the DOF requesting guidance about unfunded pension and retiree health liabilities being enforceable obligations of the Successor Agency of a Redevelopment Agency as modified with respect to identification of the Successor Agency as opposed to the City in paragraph two (2). Approved by the following voice vote: AYES: Boardmembers Addiego, Christensen, Farrales and Scannell, Vice Chairperson Porterfield and Chairperson Cullen. NOES: Boardmember Beaudin. ABSTAIN: None. ABSENT: None

4. Future Agenda Items.
  - a. Report on any determination by the State of California Department of Finance on unfunded pension and liabilities being an enforceable obligation of the Successor Agency of a Redevelopment Agency

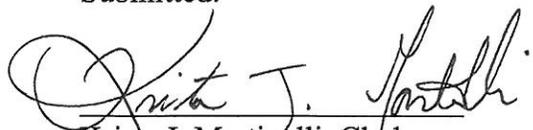
At Boardmember Christensen's request, the Board agreed to place an item pertaining to RPTTF tax distribution methodology and implications for Prop 1A on the December 11, 2012 Regular Meeting Agenda

#### ADJOURNMENT

Motion– Boardmember Beaudin/Second– Boardmember Scannell: to adjourn the meeting. Unanimously approved by voice vote.

Pursuant to the above motion, Chairperson Cullen adjourned the meeting at 2:29 p.m.

Submitted:

  
\_\_\_\_\_  
Krista J. Martinelli, Clerk  
City of South San Francisco

Approved:

\_\_\_\_\_  
Neil Cullen, Chairperson  
Oversight Board for the Successor Agency to the  
City of South San Francisco Redevelopment  
Agency



# Redevelopment Successor Agency Oversight Board Staff Report

DATE: December 11, 2012

TO: Members of the Oversight Board

FROM: Jim Steele, Finance Director

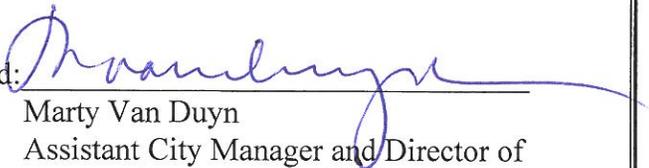
SUBJECT: DISCUSSION ITEM ON PROPOSITION 1A IMPLICATIONS OF COUNTY  
CONTROLLER'S METHODOLOGY FOR ALLOCATING REDEVELOPMENT  
PROPERTY TAX TRUST FUND (RPTTF) PROCEEDS

The following attachments are being transmitted from Boardperson Christensen regarding the implications for how the State Department of Finance interpretation of paying taxing entities through the Redevelopment Property Tax Trust Fund (RPTTF) process may be in violation of Proposition 1A's constitutional provisions of not altering the way property taxes are allocated without a 2/3 vote of the Legislature.

By: \_\_\_\_\_

  
Jim Steele  
Finance Director

Approved: \_\_\_\_\_

  
Marty Van Duyn  
Assistant City Manager and Director of  
Economic and Community Development

## Attachments:

- I. Background information on the issue prepared by Boardperson Christensen
- II. Fiscal Consultant analysis of the impacts to San Mateo County taxing entities
- III. Pre-AB 1484 white paper from League of California Cities on the proper way to allocate RPTTF funds

**I. Consideration of joining a coalition to seek legal advice on the constitutionality of the calculation method County Auditor/Controller is using to determine taxing entities' share of the RPTTF**

**Background:**

In November 2004, the voters of California approved Proposition 1A, an amendment to the California state constitution intended to restore predictability and stability to local government budgets. The measure, among other things, prohibits the Legislature from altering the share of property tax revenues that cities, county and special districts are entitled to under the ordinary pro rata share of property taxes allocated under the Revenue and Tax Code, commonly known as an AB8 share. It did allow such shifting of revenues only if the Legislature declared an emergency and approved the measure authorizing the tax shift with 2/3 approval in each house.

As explained in detail in the attached paper, the method the Department of Finance has advised counties to use in calculating payments appears to be a violation of Prop 1A. The Legislative Analyst's Office and the California State Association of County Auditors have both questioned the methodology being used by the Department of Finance.

Initially, AB 26 required the County Auditors to use the funds in the RPTTF first to pay the enforceable obligations of the former RDA and the Administrative Cost Allowance for the Successor Agency. Next, the Auditor was to apply each taxing entities' AB8 percentage share to the funds remaining in the RPTTF. If a taxing entity had a pass through that exceeded the amount under the AB 8 calculation, the pass through was to be capped at the AB8 share amount. If a taxing entity had a pass through agreement that was less than its calculated AB8 share, additional funds were to be allocated to the taxing entity so that the revenues received equaled the AB8 share. This initial methodology was revenue neutral to all taxing entities, and would have been consistent with Proposition 1A.

After AB 1484 was passed, however, the Department of Finance has taken the position that this distribution method only applies to distribution of funds "such as the proceeds from asset sales" and that pass through payments must be honored with no reductions. If pass through payments are honored without regard to the AB8 share, the result is that some taxing entities are receiving more than their AB8 share and others are receiving less than their share, which appears to be a tax shift and/or an alteration of taxing entities' share of property taxes contrary to Prop 1A.

Countywide, the total tax shift is \$5.4M to the County and this amount is being taken away from cities, schools and other taxing entities. Specifically, in South San Francisco, the shift is \$2.3M and the major losers in this calculation are the SSF Unified School District (\$1,415,930) the City of SSF (\$612,143), the College District (\$141,072), the Colma Creek Flood Control Project (\$57,252), and the County Office of Education (\$42,809). (See attached Countywide and SSF analysis prepared by Don Fraser).

The College District is proposing that a coalition be formed in the County to jointly approach our local legislators to seek an Attorney General's opinion on the constitutionality of the current method of calculations. This coalition could include school districts, oversight boards, successor agencies and other taxing entities.

**Action:** Discuss the Prop 1A issue and decide whether to seek out other interested taxing entities to jointly seek legal advice on the constitutionality of the calculation method being used to calculate taxing entities share of RPTTF. The Board could, for example, designate a Boardperson and a staff person to seek input from other taxing entities and report back to legal counsel and the Board.

## SUMMARY OF HAIRCUT IMPACTS - LARGE DISTRICTS

| General<br>County   | Free<br>Library | Sequoia<br>High | SM<br>College | Office<br>Of Education | Redwood<br>City Elementary | San<br>Mateo High | Cities              |
|---------------------|-----------------|-----------------|---------------|------------------------|----------------------------|-------------------|---------------------|
| Belmont             | 155,841         | (8,686)         | (24,140)      | (10,482)               | (5,459)                    | 0                 | (25,236)            |
| Brisbane            | 27,794          | 4,051           | 0             | (2,910)                | (1,185)                    | 0                 | (8,930)             |
| East Palo Alto      | (18,765)        | (12,959)        | (33,806)      | (12,862)               | (12,831)                   | 0                 | (191,076)           |
| Menlo Park          | 758,905         | 0               | (25,879)      | 38,276                 | (4,873)                    | (7,498)           | (668,981)           |
| Millbrae            | 343,080         | (22,955)        | (87,359)      | (36,663)               | (19,080)                   | 0                 | (90,572)            |
| Redwood City        | 1,172,741       | 0               | (148,567)     | (84,561)               | (32,847)                   | (294,164)         | (548,061)           |
| San Bruno           | (70,185)        | 0               | 0             | (19,252)               | 71,119                     | 132,627           | (38,759)            |
| San Carlos          | 675,618         | 98,486          | (100,722)     | (82,355)               | (21,393)                   | 0                 | (258,572)           |
| San Mateo           | (16,069)        | 0               | 0             | (4,397)                | 24,319                     | 55,498            | (35,090)            |
| South San Francisco | 2,325,961       | 0               | 0             | (141,072)              | (42,809)                   | 0                 | (612,143)           |
| Total               | 5,354,920       | 57,937          | (420,475)     | (356,278)              | (45,039)                   | (323,944)         | 188,125 (2,477,420) |

South San Francisco Successor Agency

**IMPACT FROM NOT APPLYING THE SECTION 34188 "HAIRCUT"**

|  | May<br>Impact | June<br>Impact | Total       |
|--|---------------|----------------|-------------|
| <i>Entities with Gains From Pass Through</i> |               |                |             |
| GENERAL COUNTY TAX                           | 1,850,134     | 475,827        | 2,325,961   |
| WILLOW GARDENS PKS-PKWYS MNT                 | 588           | 0              | 588         |
| Total  | 1,850,722     | 475,827        | 2,326,549   |
| <i>Entities with Losses</i>                  |               |                |             |
| GENERAL COUNTY TAX                           |               | 0              | 0           |
| CITY OF SOUTH SAN FRANCISCO                  | (493,249)     | (118,895)      | (612,143)   |
| SO SAN FRAN UNIFIED GENL PUR                 | (1,164,089)   | (287,841)      | (1,451,930) |
| SM JR COLLEGE GEN PUR                        | (99,906)      | (41,166)       | (141,072)   |
| COLMA CR FLOOD CONTROL ZONE                  | (6,825)       | (1,706)        | (8,531)     |
| COLMA CR FLOOD CONT SUB ZN 3                 | (2,960)       | (710)          | (3,670)     |
| COLMA CR FLOOD CONT SUB ZN 2                 | (32,387)      | (8,204)        | (40,591)    |
| COLMA CR FLOOD CONT SUB ZN 1                 | (2,801)       | (660)          | (3,460)     |
| WILLOW GARDENS PKS-PKWYS MNT                 | 0             | (250)          | (250)       |
| BAY AREA AIR QUALITY MANAGEMENT              | (6,515)       | (1,584)        | (8,099)     |
| COUNTY HARBOR DISTRICT                       | (11,111)      | (2,694)        | (13,805)    |
| RESOURCE CONSERVATION DISTRICT               | (151)         | (35)           | (187)       |
| COUNTY EDUCATION TAX                         | (30,728)      | (12,081)       | (42,809)    |
| Total  | (1,850,722)   | (475,827)      | (2,326,549) |

Prepared by the League  
prior to the passage of 1484



1400 K Street, Suite 400 • Sacramento, California 95814  
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Administration of Passthrough Payments from the  
Redevelopment Property Tax Trust Fund under ABx1 26

**GENERAL DISCLAIMER:** This document represents an attempt to interpret the requirements of AB x1 26 as modified by the California Supreme Court in *California Redevelopment Association v. Matosantos*. This document does not constitute legal advice. Given the significant ambiguities, conflicts, and murkiness of AB x1 26, it is important to consult with legal counsel regarding any issues discussed in this document. The statements in this document reflect the consensus or recommendation of the subgroup that drafted this document in consultation with the members of the entire Working Group. No statement in this document should be attributed to any individual member of the subgroup or the Working Group. This document represents an analysis as of the date set forth in the footer below. This document will be updated as needed to reflect legislative changes and revised analyses. If you have questions or comments regarding this document, please direct them to Patrick Whitnell, General Counsel for the League of California Cities, at [pwhitnell@cacities.org](mailto:pwhitnell@cacities.org).

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The Post-Redevelopment Working Group (“Working Group”) of the League of California Cities (the “League”) provides this Statement of Position (referred to herein as the “white paper” or “position paper”) to (1) explain the Working Group’s position concerning the disbursements from the Redevelopment Property Tax Trust Fund (“RPTTF”) to pay for statutory and contractual passthrough payments as set forth in ABx1 26, and (2) assert that all California cities must receive the full property tax allocation assigned to them as required by State constitutional and statutory law.

The elimination of redevelopment has substantially reduced the revenues available to California cities for important projects designed to produce jobs, economic development, affordable housing, and valued infrastructure. While the revenue losses compromise the ability of cities to achieve these important goals, a portion of the lost revenue should be returned to cities in the form of increased property tax revenues.

In this regard, the Working Group supports the distribution methodology from the RPTTF for passthrough payments under ABx1 26 that has been identified by both the Legislative Analyst Office (“LAO”) in *Unwinding Redevelopment*,<sup>1</sup> and the California State Association of County Auditors (“Auditor’s Association”) through its Accounting Standards Committee, in *Draft Uniform Guidelines for the Implementation of Assembly Bill No. 26*.<sup>2</sup> The LAO and Auditor’s Association, along with the Working Group, read ABx1 26 so as to require property tax distributions for each taxing entity to equal the property tax share assigned to that entity under the ordinary pro-rata share of property tax revenues allocated under applicable provisions in the Revenue and Taxation Code, commonly referred to as an “AB 8” share, and referred to herein as the “AB 8 Tax Share Reading.”

Under the AB 8 Tax Share Reading, passthrough payments to taxing agencies are adjusted so the overall property taxes paid to each taxing agency matches the ratios set by law under AB 8 allocations. The Working Group supports the AB 8 Tax Share Reading because it achieves a result that not only complies with the plain language of ABx1 26, but also conforms to the requirements of Article XIII, Section 25.5(a)(3) of the California Constitution, added by Proposition 1A in 2004, which requires 2/3 approval by both houses of the Legislature to enact a law that reallocates ad valorem property tax revenues among local taxing entities.

The LAO appears to agree that the constitutionally sound interpretation of ABx1 26 requires the implementation of the AB 8 Tax Share Reading. Nevertheless, it appears that the California Department of Finance (“DOF”) takes a contrary and, in the Working Group’s opinion, unsupported reading of ABx1 26 with respect to passthrough payment provisions. Specifically, DOF’s contrary reading appears in Answer 4 to *Additional Frequently Asked Questions 2-29-2012*, posted on DOF’s website (“FAQ Reading”), which contends that passthrough payments are not subject to adjustment under Health and Safety Code section 34188.<sup>3</sup>

As more specifically explained in this white paper, and the reports from the LAO and Auditor’s Association cited herein, the Working Group asserts that the FAQ Reading from DOF should be rejected because it misreads the plain language of ABx1 26, conflicts with the California Constitution, and is mathematically unworkable.

## **I. THE AB 8 TAX SHARE READING FOLLOWS THE LANGUAGE OF ABx1 26 AND SATISFIES THE STATE CONSTITUTION**

<sup>1</sup> See, pages 19 and 20 of the LAO report.

<sup>2</sup> See, pages 23 and 24 of the Auditor’s Association report.

<sup>3</sup> See DOF Website link:

[http://www.dof.ca.gov/assembly\\_bills\\_2627/documents/RDA\\_New\\_FAQs\\_2-2\\_Exhibit5.pdf](http://www.dof.ca.gov/assembly_bills_2627/documents/RDA_New_FAQs_2-2_Exhibit5.pdf).

Pursuant to ABx1 26, the former tax increment of each dissolved redevelopment agency is deposited into the RPTTF. Distributions are made from the RPTTF based on the property tax share of each taxing entity (*i.e.*, the AB 8 share), as described in the first sentence of Health and Safety Code section 34188:<sup>4</sup>

“[A]ll distributions of property tax revenues...to **each taxing entity** shall be in an amount proportionate to its share of property tax revenues in the tax rate area in that fiscal year....”

(Emphasis added.) The AB 8 share payable to each taxing entity is taken from the net amount in the RPTTF after payment of enforceable obligations and the administrative allowance (“Net RPTTF Balance”):

“For distributions from the Redevelopment Property Tax Trust Fund, the share of **each taxing entity** shall be applied to the amount of property tax available in the Redevelopment Property Tax Trust Fund after deducting the amount of any distributions under paragraphs (2)<sup>5</sup> and (3)<sup>6</sup> of subdivision (a) of Section 34183.”

(Section 34188(a)(1) [emphasis added].)

These quoted provisions describe a “Standard Distribution Rule” through which each taxing entity takes its AB 8 share of the Net RPTTF Balance. By referencing “each taxing entity” in these provisions, the Legislature signaled its intention that the provisions would apply equally to taxing entities with and without passthrough obligations.

Furthermore, Section 34188(a)(2) describes how to implement the Standard Distribution Rule “for each taxing entity that receives passthrough payments.” Paragraph (2) places a ceiling on the amount that is payable as a passthrough pursuant to Section 34183(a)(1):

“For each taxing entity that receives passthrough payments, that agency shall receive the amount of any passthrough payments identified under paragraph (1) of subdivision (a) of Section 34183, in an amount **not to exceed** the amount that it would receive pursuant to this section in the absence of a passthrough agreement.”

(Section 34188(a)(2) [emphasis added].)

<sup>4</sup> Unless otherwise indicated, all statutory references are to the California Health and Safety Code.

<sup>5</sup> Amounts payable toward enforceable obligations based on an approved Recognized Obligation Payment Schedule.

<sup>6</sup> Amounts payable toward the administrative cost allowance.

While such taxing entities can continue to receive passthrough payments, the payment is capped according to the Standard Distribution Rule (*i.e.*, the entity's AB 8 share of the Net RPTTF Balance). However, the entity will receive a supplemental payment from the RPTTF when the amount of its passthrough is less than the amount that would be payable under the Standard Distribution Rule:

“However, to the extent that the passthrough payments received by the taxing entity are less than the amount that the taxing entity would receive pursuant to this section in the absence of a passthrough agreement, the taxing entity shall receive an additional payment that is equivalent to the difference between those amounts.”

(Section 34188(a)(2).)

In this manner, Section 34188(a)(2) assures that taxing entities with passthroughs receive payments from the Net RPTTF Balance equal to their AB 8 share by augmenting the passthrough payments or, when needed, adjusting the payments downward. Moreover, the AB 8 share paid to each taxing entity (with or without a passthrough) should total 100% of the Net RPTTF Balance.

Not only does AB 8 Tax Share Reading match the language in ABx1 26, this interpretation allows ABx1 26 to withstand constitutional scrutiny under Article XIII, Section 25.5(a)(3). As noted in the LAO report, ABx1 26 was adopted only by a simple majority from both houses of the Legislature. ABx1 26 did not receive a 2/3 majority from each house of the Legislature, which is required constitutionally for the State to reallocate property tax revenues in a manner that would alter their ordinary AB 8 share. As such, the AB 8 Tax Share Reading is the only means to constitutionally implement passthrough payment provisions in ABx1 26.

It is in this regard that any priority given to passthrough payments provided for in Section 34183 — even if to recognize those situations in which a taxing entity may have pledged proceeds from passthrough payments to repay that taxing entity's indebtedness obligations — must yield to Section 34188 and the AB 8 Tax Share Reading. Article XIII, section 25.5(a)(3). It trumps any intent by the Legislature to preserve some sort of priority for passthrough payments in ABx1 26, and therefore mandates the AB 8 Tax Share Reading.<sup>7</sup>

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<sup>7</sup> The Working Group is aware that taxing entities may have issued debt that pledged as security for repayment of that debt passthrough payments that, had the Legislature not dissolved redevelopment agencies with the enactment of ABx1 26, would have been disbursed from the redevelopment agencies to the taxing entities to cover costs related to redevelopment in accordance with applicable statutory or contractual passthrough provisions. To the extent that application of Section 34188 would produce a reduction in the amount of passthrough payments such that insufficient funds would be available to meet debt service on this indebtedness, a holder

## II. DOF'S FAQ READING CONFLICTS WITH THE PLAIN LANGUAGE OF ABx1 26 AND WOULD PRODUCE UNCONSTITUTIONAL RESULTS

The FAQ Reading, found in *Additional Frequently Asked Questions 2-29-2012*, conflicts with the plain language of ABx1 26, violates Article XIII, Section 25.5(a)(3), and it is mathematically impossible to implement. As such, it should be rejected.

According to the FAQ Reading, Section 34188(a)(2) does not cap the amount of property taxes payable to a taxing entity as a passthrough pursuant to Section 34183(a)(1). Rather, the DOF posits that Section 34188(a)(2) applies only to "the distribution of other money, such as the proceeds from asset sales." Yet, the introductory sentence of Section 34188 indicates that its rules apply to "**all distributions of property tax revenues and other moneys pursuant to this part.**" (Part 1.85, added by ABx1 26, consists of Sections 34170-34191). In the Working Group's opinion, the FAQ Reading is wrong. By its terms, Section 34188 applies to "all distributions of property tax," covered by "this part," which, therefore, includes passthrough payments described in Section 34183(a)(1).

Moreover, Section 34188(a)(2) caps the "amount of any passthrough payments" made to a taxing entity to "an amount not to exceed the amount it would receive pursuant to this section in the absence of a passthrough." The FAQ Reading appears to render meaningless the language in ABx1 26 concerning this distribution cap.

Additionally, the FAQ Reading appears to advocate the distribution of property taxes comprised of former tax increment so that some taxing entities (those with passthrough payments) would receive distributions of property tax exceeding their AB 8 shares, while others (those without passthrough payments) would receive distributions falling below their AB 8 shares. If this situation were to result, then ABx1 26 violates Article XIII, Section 25.5(a)(3) of the California Constitution, because the Legislature would have reallocated the distribution of property taxes without obtaining the requisite 2/3 vote approval from each house of the Legislature.

Finally, the FAQ Reading is mathematically unworkable. Section 34188(a)(1) provides that "each taxing entity shall" receive a distribution, based on its tax share, drawn from the "Redevelopment Property Tax Trust Fund after deducting the amount of any distributions under paragraphs (2) and (3) of subdivision (a) of Section 34183." The described deductions do not include passthrough payments that are governed by Section 34183(a)(1). Of course, it is impossible (as would occur under the FAQ Reading) to first remove a slice from the RPTTF "pie"

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of such debt may need to negotiate or seek a remedy as appropriate to obtain timely payment from the taxing entity that issued the debt.

consisting of passthrough payments, and then to distribute the pie once again to “each taxing entity” as though the passthrough slice still remained in place.

### **III. CONCLUSION**

For the reasons discussed above, the Working Group agrees with the LAO and Auditor’s Association, and their respective reports cited in this white paper, that the AB 8 Tax Share Reading implements the plain language of ABx1 26, satisfies the California Constitution with respect to the passthrough provisions in ABx1 26, and uses a methodology that properly distributes property taxes from RPTTF to the taxing entities.

\* \* \*

December 11, 2012

TO: Members of the Oversight Board

FROM: Neil Cullen, Chairman of the Oversight Board

SUBJECT:

- a) Discussion of the State of California Department of Finance (DOF) response to the Chairman of the Oversight Board's letter requesting guidance on unfunded pension and retirement health liabilities (unfunded liabilities) being an enforceable obligation of the Successor Agency (SA) of a South San Francisco Redevelopment Agency (RDA).
- b) Possible Oversight Board (OB) direction to staff on developing a request to include unfunded liabilities on a subsequent Recognized Obligations Payment Schedule (ROPS).

#### RECOMMENDATION

After discussing the DOF's response to the Chairman's letter, consider the parameters to be used by staff in preparing a request to include unfunded liabilities on a subsequent ROPS.

#### BACKGROUND

The OB deferred including payment for unfunded liabilities in past ROPS pending an opinion from DOF because of the legal uncertainty regarding whether AB1x 26 allowed reimbursement for unfunded liabilities associated with city employees who performed services for the former RDA, as compared to direct RDA employees.

The OB authorized the Chairman to send a letter to DOF requesting clarification on including unfunded liabilities in future ROPS, and DOF responded via Mr. Steve Szalay's letter to the Chairman. (Letters attached).

#### DISCUSSION

Mr. Szalay opined that in most cases unfunded liabilities would be considered by DOF to be enforceable obligations, regardless of whether the employees were employed by the RDA or were city employees performing work for the RDA. However, before making a final determination on South San Francisco's ROPS, DOF will:

- a) Review the Memorandum of Understandings (MOU's) that covered the employees; and
- b) Determine if the charges were reasonable based on:
  - 1) The unfunded liability being proportionate to the percentage of work the employee dedicated to the RDA; and
  - 2) the tasks performed by the employees that had their salaries paid all or in part with RDA funds.

Jim Steele's memo of April 13, 2012, provided the OB with a summary of positions and wages charged based on the City's payroll system for 2011, and estimated costs for 2009 and 2010 as Jim explained that the City's payroll system was not set up to track the number of hours worked per position until 2011; and the explanation of line 71 of the draft ROPS gave the method used to calculate an amount based on CalPERS reports of unfunded pension obligations (copies attached)

However, the information provided does not appear to meet DOF's criteria, and the assumption is that DOF would reject an unfunded liabilities claim if presented based on the information currently available to the OB.

There appears to be at least two approaches for determining what unfunded liabilities should be included in the ROPS:

- 1) Staff develops and brings to the OB their methodology for determining the unfunded liabilities based on the DOF letter, and then the OB reviews, comments and possibly modifies before approving, an unfunded liability line item on the ROPS.
- 2) The OB discusses the contents of DOF's letter, provides direction to staff, and then staff develops and brings the unfunded liability methodology to the OB for its consideration.

The latter option appears to provide the best use of staff time, as there is significant work to be done by staff given the number of different MOU's that may cover the employees listed in Jim's April memo, and then providing the information about the tasks that the employees were doing on behalf of the RDA.

It may take the OB more than one meeting to discuss and come to a consensus on direction to staff. However, beginning this discussion now allows more time to reach a consensus. The next ROPS is due in March 2013 and the complexity of the issue may delay including an unfunded liability line item in this ROPS.

#### FISCAL IMPACT

There is no fiscal impact by discussing DOF's letter. There will be a fiscal impact in terms of staff time charged to develop a methodology to be used and to calculate an appropriate payment to the SA for past unfunded liabilities, and to the other taxing agencies that receives funding from the Redevelopment Property Tax Trust Fund (RPTTF) as a payment to the SA for unfunded liabilities will reduce the amount available in the RPTTF that is used to make payments to the other taxing agencies.

Counsel for the Oversight Board has reviewed this report.

Neil R. Cullen



Chairman- South San Francisco Redevelopment Successor Agency Oversight Board

Enclosures:

1. Letter to DOF, dated November 13, 2012
2. Letter from DOF, dated November 20, 2012
3. Jim Steele's memo of April 13, 2012 & Line 71 explanation

November 13, 2012

Mr. Steve Szalay  
Local Government Unit  
Department of Finance  
915 L Street  
Sacramento, CA 95814-3706

RE: Request for Direction from the Department of Finance Regarding the Inclusion of Past Unfunded Pension and Benefit Liabilities as Part of the South San Francisco Recognized Obligations Payment Schedule

Dear Mr. Szalay:

I am the current chairman of the Oversight Board (OB) to the Successor Agency of the former South San Francisco Redevelopment Agency (RDA) and am writing on behalf of the OB to request your assistance in clarifying the Department of Finance's (DOF) position on including past unfunded pension and benefit liabilities as part of a Recognized Obligations Payment Schedule (ROPS).

The Successor Agency (SA) has requested that an item be included in its ROPS to reimburse the City for unfunded CalPERS pension and retiree health benefit costs associated with staff time charged in the past to the SSFRDA by City employees. The Successor Agency's argument is that City employees should be considered as employees of the RDA within the meaning of applicable statutes; and therefore unfunded pension and benefit costs associated with staff that provided services to the RDA prior to its dissolution should be considered enforceable obligations.

The OB deferred including payment for such costs in past ROPS because of the legal uncertainty regarding whether AB1x 26 allowed reimbursement for unfunded liabilities associated with City employees who performed services for the former RDA, as compared to direct RDA employees. AB1x 26 defined the term "enforceable obligation" for former redevelopment agencies to include: "legally enforceable payments required in connection with the agencies' employees, including, but not limited to, pension payments, pension obligation debt service, unemployment payments, or other obligations conferred through a collective bargaining agreement." (Health & Safety Code Section 34171(d)(1)(C).) Other provisions in AB1x 26 also referenced employees of former redevelopment agencies without clearly stating whether or not these references were intended to apply to City employees who were assigned to provide services to a redevelopment agency and whose time was charged to the agency, or just direct agency employees. (See Health & Safety Code Section 34179(a)(7) and Section 34190.) Earlier this year, the Department of Finance posted information on its website regarding this issue, but did not provide clear guidance regarding the question whether unfunded liabilities associated with city employees who supported former redevelopment agencies can be treated as enforceable obligations.

AB 1484, enacted in June 2012, added language to Health & Safety Code Section 34171(d)(1)(C) that modified the definition of "enforceable obligation" to include "costs to fulfill collective bargaining agreements for layoffs or terminations of city employees who performed

work directly on behalf of the former redevelopment agency." However, this language seems to cover only those employees whose services were no longer needed following the agency's dissolution. Section 34179(a)(7) also was amended to expressly recognize a distinction between employees of the former redevelopment agency and city employees who performed administrative duties for the former redevelopment agency, in the context of qualifications for the employee representatives appointed to oversight boards. However, these statutory changes did not unambiguously address the situation presented in South San Francisco, where City employees supported the RDA and typically had a portion of their salaries funded by RDA revenues, but were also doing regular city business.

My understanding is that the DOF may review all actions of the oversight boards and then has 40 days to approve, reject, or modify these actions. Our OB has several options to consider:

- a) wait for a decision by the DOF on the inclusion of unfunded obligations in another successor agency's ROPS that may or may not be similar to South San Francisco's situation;
- b) make a determination to include or exclude past unfunded obligations in a ROPS and wait for DOF's review or the SA's appeal if the OB's action is contrary to their position; or
- c) request DOF's direction "upfront" and then proceed accordingly.

Requesting direction "upfront" appears to the OB to be the most appropriate option as past comments by the DOF lead the OB to believe that you are looking for statewide consistency.

In closing, I believe both the South San Francisco OB and the City's Successor Agency have worked cooperatively in meeting the intent of the legislation that dissolved redevelopment agencies statewide. I believe that requesting DOF direction regarding the issues presented in this letter is the most appropriate course of action to facilitate an expeditious wind-down of the affairs of this Redevelopment Agency for the benefit of all the affected local taxing entities.

Thank you in advance for considering my request and look forward to any direction that you can provide the Oversight Board.

Very truly yours,



Neil R. Cullen

Chairman Oversight Board of the Successor Agency to the South San Francisco Redevelopment Agency



November 20, 2012

Mr. Neil Cullen, Chairman  
South San Francisco Oversight Board  
P.O. Box 711  
South San Francisco, CA 94083

Dear Mr. Cullen:

This letter is in response to the Oversight Board's request for clarification on the Department of Finance's (Finace) position regarding the inclusion of past unfunded pension and benefit liabilities in the Recognized Obligation Payment Schedule (ROPS).

As Finance understands the situation, the Successor Agency (SA) of the former South San Francisco Redevelopment Agency (RDA) requested to include an issue in the ROPS to reimburse the City of South San Francisco for the unfunded pension and retiree health costs associated with staff time that had previously been charged to the RDA by city employees.

Finance expects that in most cases unfunded costs for pensions and other employee benefits will be determined to be enforceable obligations, regardless of whether the employees were employed by the RDA or were city employees performing work for the RDA. However, the specific requirements of Memorandums of Understanding or other contractual agreements related to the employees in question will have to be reviewed before a final determination can be made.

Specifically, in regards to the South San Francisco SA's intent to include the alleged unfunded pension and retiree health costs in the ROPS, Finance does not yet have an official position. If such costs are included on ROPS 4, Finance will examine whether the repayment is reasonable. In particular, we will examine whether the repayments are proportionate to the percentage of work time that the impacted employees dedicated to the former RDA, as well as the tasks performed by the employees while their salaries were being funded by the former RDA.

Should you have any further questions please direct your inquiries to Justyn Howard, Assistant Program Budget Manager, at (916) 445-1546.

Sincerely,



STEVE SZALAY  
Local Government Consultant

cc: Ms. Krista Martinelli, City Clerk, South San Francisco

# Memo

**To:** Honorable Oversight Board to the South San Francisco Successor Agency  
**From:** Jim Steele, Finance Director  
**Date:** April 13, 2012  
**Re:** Employee Charges to SSF RDA, 2009-2011

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Attached for the Board's information are the full-time equivalent (FTE) employee charges to the former South San Francisco Redevelopment Agency (RDA) over the last three years. These lists were generated through the City's payroll system, and show each employee's department, position title, wage amount, and number of hours charged directly to the RDA. Employee names have been omitted for this exercise, but can be supplied upon request.

Please note the following:

- 1) For the 2011 calendar year, the hours shown are the actual numbers as reported by the payroll system;
- 2) During calendar years 2010 and 2009, the payroll system was not set up to track the number of hours worked by position: for those years the FTE numbers are estimates, derived by using the percentage of FTE's to total wages in 2011.

| Department       | Position                                     | Age<br>Amount | Hours<br>Charged |
|------------------|--|---------------|------------------|
| CITY CLERK       | DEPUTY CITY CLERK                            | 51,596.42     | 1,800            |
| CITY CLERK       | MISC HOURLY - CITY CLERK                     | 226.40        | 8                |
| ECD ADMIN        | ASST CITY MANAGER                            | 79,464.60     | 786              |
| ECD ADMIN        | ECONOMIC & COMMUNITY DEVELOPMENT COORDINATOR | 114,691.20    | 2,080            |
| ECD ADMIN        | MANAGEMENT ANALYST I                         | 8,067.93      | 234              |
| ECD ADMIN        | MISC ECD-ADM                                 | 6,787.50      | 272              |
| ECD CDBG         | MANAGER OF HOUSING & REDEVEL                 | 36,146.41     | 549              |
| ECD CDBG         | MISC HOURLY - PD COPPS                       | 1,408.00      | 152              |
| ECD PLANNING     | PRINCIPAL PLANNER                            | 37,670.69     | 717              |
| ECD REDEVELPMNT  | MISC HOURLY - REDEV                          | 2,600.00      | 104              |
| ECD REDEVELPMNT  | MISC HOURLY - REDEV                          | 1,558.00      | 82               |
| FIN ACCTG        | ACCOUNTANT I                                 | 73,715.20     | 2,080            |
| FIN ACCTG        | DATA BUSINESS SYSTEMS SPECIALIST             | 63,362.98     | 2,072            |
| FIN ADMIN        | DIRECTOR OF FINANCE                          | 7,012.00      | 72               |
| FIN BUDGET       | SENIOR FINANCIAL ANALYST                     | 22,680.01     | 480              |
| IT               | INFORMATION SYSTEMS ADMINISTRATOR            | 116,646.40    | 2,168            |
| LIB LEARNING CTR | LITERACY PROGRAM MANAGER                     | 12,182.04     | 274              |
| LIB LEARNING CTR | LITERACY SERVICES COORDINATOR                | 38,315.98     | 1,104            |
| PD PATROL        | POLICE OFFICER                               | 12,796.08     | 258              |
| PD PATROL        | POLICE OFFICER                               | 89,507.94     | 1,884            |
| PD PATROL        | POLICE OFFICER                               | 99,437.67     | 2,172            |
| PW ELECTRICAL    | ELECTRICAL TECHNICIAN                        | 143.48        | 4                |
| PW ELECTRICAL    | ELECTRICAL TECHNICIAN                        | 83.31         | 3                |
| PW ELECTRICAL    | LEAD ELECTRICAL TECHNICIAN                   | 142.83        | 3                |
| PW ELECTRICAL    | MISC HOURLY - PW SIGNALS                     | 504.90        | 11               |
| PW ENGINEERING   | ADMINISTRATIVE ASSISTANT I                   | 517.23        | 19               |
| PW ENGINEERING   | CITY ENGINEER                                | 1,663.68      | 24               |
| PW ENGINEERING   | ENGINEERING TECHNICIAN                       | 1,750.90      | 52               |
| PW ENGINEERING   | OFFICE SPECIALIST                            | 981.12        | 37               |
| PW ENGINEERING   | PUBLIC WORKS INSPECTOR                       | 38,749.31     | 818              |
| PW ENGINEERING   | SR CIVIL ENGINEER                            | 5,417.70      | 84               |
| PW ENGINEERING   | SR CIVIL ENGINEER                            | 2,658.60      | 42               |
| PW SEWER MAINT   | PUBLIC WORKS MAINT WORKER                    | 206.56        | 8                |
| PW STREETS       | EQUIPMENT OPERATOR                           | 812.05        | 24               |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 26,838.62     | 1,228            |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 28,308.70     | 1,295            |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 666.91        | 24               |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 2,328.52      | 92               |
| PW STREETS       | SR PUBLIC WORKS MAINT WORKER                 | 258.20        | 16               |
| PW STREETS       | SR PUBLIC WORKS MAINT WORKER                 | 232.24        | 8                |
| PW STREETS       | SWEEPER OPERATOR                             | 81.18         | 3                |
| REC BLDG MAINT   | BLDG MAINT CRAFTSWORKER                      | 32.17         | 1                |
| REC BLDG MAINT   | BLDG MAINT CRAFTSWORKER                      | 263.79        | 8                |
| REC BLDG MAINT   | BLDG MAINT CUSTODIAN                         | 651.96        | 36               |
| REC BLDG MAINT   | BLDG MAINT CUSTODIAN                         | 78.51         | 4                |
| REC PARKS        | MISCELLANEOUS HOURLY                         | 620.16        | 19               |
| REC PARKS        | PARK MAINT WORKER                            | 258.20        | 10               |
| REC PARKS        | PARK MAINT WORKER                            | 52,812.47     | 1,948            |
| REC PARKS        | PARK MAINT WORKER                            | 207.00        | 12               |
| REC PARKS        | PARK MAINT WORKER                            | 81.33         | 3                |

|               |             |                     |               |
|---------------|-------------|---------------------|---------------|
| <b>Totals</b> | <b>2011</b> | <b>1,043,225.08</b> | <b>25,181</b> |
|               |             | <b>Wages</b>        | <b>Hrs.</b>   |

|          |                  |
|----------|------------------|
| Est. FTE | <b>12.11</b>     |
| Avg. \$  | <b>86,173.19</b> |
| per FTE  |                  |

| Department       | Position                                     | Page<br>Amount |
|------------------|--|----------------|
| CITY CLERK       | ASSISTANT CITY CLERK                         | 10,308.00      |
| CITY CLERK       | DEPUTY CITY CLERK                            | 53,145.15      |
| ECD ADMIN        | ADMINISTRATIVE ASSISTANT II                  | 4,681.80       |
| ECD ADMIN        | ASST CITY MANAGER                            | 70,611.35      |
| ECD ADMIN        | ECONOMIC & COMMUNITY DEVELOPMENT COORDINATOR | 109,764.40     |
| ECD ANIP         | ANIP CONSTRUCTION MANAGER                    | 6,738.96       |
| ECD CDBG         | MANAGER OF HOUSING & REDEVEL                 | 22,636.20      |
| ECD CDBG         | MISC HOURLY - PD COPPS                       | 528.00         |
| ECD PARKING      | PARKING METER COLLECTOR - REPAIR WRKR        | 554.81         |
| ECD PLANNING     | PRINCIPAL PLANNER                            | 30,492.31      |
| ECD REDEVELPMNT  | MISC HOURLY - REDEV                          | 2,888.00       |
| FIN ACCTG        | ACCOUNTANT I                                 | 72,987.24      |
| FIN ACCTG        | DATA BUSINESS SYSTEMS SPECIALIST             | 56,348.97      |
| FIN BUDGET       | SENIOR FINANCIAL ANALYST                     | 93,415.24      |
| IT               | CONSULTANT                                   | 353.84         |
| IT               | INFORMATION SYSTEMS ADMINISTRATOR            | 115,512.80     |
| LIB LEARNING CTR | LITERACY PROGRAM MANAGER                     | 8,458.88       |
| LIB LEARNING CTR | LITERACY SERVICES COORDINATOR                | 38,121.50      |
| PD CMTY RELATION | MISC HOURLY - PD COPPS                       | 256.00         |
| PD CMTY RELATION | POLICE CORPORAL                              | 8,195.17       |
| PD PATROL        | POLICE OFFICER                               | 107,125.81     |
| PD PATROL        | POLICE OFFICER                               | 81,147.47      |
| PW ELECTRICAL    | SR PUBLIC WORKS MAINT WORKER                 | 1,163.27       |
| PW ENGINEERING   | ADMINISTRATIVE ASSISTANT I                   | 1,422.87       |
| PW ENGINEERING   | ASSOC CIVIL ENGINEER                         | 4,302.71       |
| PW ENGINEERING   | ASSOC CIVIL ENGINEER                         | 2,917.68       |
| PW ENGINEERING   | ASST ENGINEER                                | 400.95         |
| PW ENGINEERING   | CITY ENGINEER                                | 10,512.16      |
| PW ENGINEERING   | ENGINEERING TECHNICIAN                       | 3,858.43       |
| PW ENGINEERING   | MISC HOURLY - ENGINEERING                    | 448.00         |
| PW ENGINEERING   | OFFICE SPECIALIST                            | 2,715.83       |
| PW ENGINEERING   | PUBLIC WORKS INSPECTOR                       | 64.53          |
| PW ENGINEERING   | PUBLIC WORKS INSPECTOR                       | 41,495.79      |
| PW ENGINEERING   | SR CIVIL ENGINEER                            | 11,071.85      |
| PW ENGINEERING   | SR CIVIL ENGINEER                            | 25,377.86      |
| PW SEWER MAINT   | LEAD PUBLIC WORKS MAINT WORK                 | 258.54         |
| PW STREETS       | EQUIPMENT OPERATOR                           | 169.18         |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 25,376.89      |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 25,250.20      |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 555.17         |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 2,665.61       |
| PW STREETS       | SR PUBLIC WORKS MAINT WORKER                 | 232.24         |
| PW STREETS       | SWEEPER OPERATOR                             | 38.66          |
| REC BLDG MAINT   | BLDG MAINT CRAFTSWORKER                      | 157.70         |
| REC BLDG MAINT   | PUBLIC WORKS SUPERVISOR                      | 64.64          |
| REC PARKS        | LEAD PARK MAINT WORKER                       | 195.82         |
| REC PARKS        | MISCELLANEOUS HOURLY                         | 111.59         |
| REC PARKS        | PARK MAINT WORKER                            | 52,487.54      |
| REC PARKS        | SR PARK MAINT WORKER                         | 216.88         |
| REC PARKS        | SR PARK MAINT WORKER                         | 335.66         |

|               |             |                     |
|---------------|-------------|---------------------|
| <b>Totals</b> | <b>2010</b> | <b>1,108,140.15</b> |
|---------------|-------------|---------------------|

|                 |              |
|-----------------|--------------|
| <b>Est. FTE</b> | <b>12.86</b> |
|-----------------|--------------|

| Department       | Position                                     | Wage Amount |
|------------------|--|-------------|
| CITY CLERK       | DEPUTY CITY CLERK                            | 36,018.21   |
| CITY CLERK       | MISC HOURLY - CITY CLERK                     | 8,793.32    |
| ECD ADMIN        | ADMINISTRATIVE ASSISTANT II                  | 34,694.28   |
| ECD ADMIN        | ASST CITY MANAGER                            | 75,894.18   |
| ECD ADMIN        | ECONOMIC & COMMUNITY DEVELOPMENT COORDINATOR | 106,566.88  |
| ECD CDBG         | MANAGER OF HOUSING & REDEVEL                 | 48,727.48   |
| ECD CDBG         | MISC HOURLY - PD COPPS                       | 1,024.00    |
| ECD PLANNING     | PRINCIPAL PLANNER                            | 35,084.44   |
| ECD REDEVELPMNT  | MISC HOURLY - REDEV                          | 4,256.00    |
| FIN ACCTG        | ACCOUNTANT I                                 | 58,634.45   |
| FIN ACCTG        | DATA BUSINESS SYSTEMS SPECIALIST             | 44,725.20   |
| FIN ADMIN        | DIRECTOR OF FINANCE                          | 1,782.84    |
| FIN BUDGET       | SENIOR FINANCIAL ANALYST                     | 88,735.20   |
| IT               | CONSULTANT                                   | 14,056.28   |
| IT               | INFORMATION SYSTEMS ADMINISTRATOR            | 96,782.40   |
| LIB LEARNING CTR | LITERACY PROGRAM MANAGER                     | 12,551.04   |
| LIB LEARNING CTR | LITERACY SERVICES COORDINATOR                | 34,302.24   |
| PD CMTY RELATION | MISC HOURLY - PD COPPS                       | 2,176.00    |
| PD CMTY RELATION | POLICE CORPORAL                              | 92,754.97   |
| PD PATROL        | POLICE OFFICER                               | 37,710.67   |
| PD PATROL        | POLICE OFFICER                               | 47,078.13   |
| PW ELECTRICAL    | ELECTRICAL TECHNICIAN                        | 928.00      |
| PW ELECTRICAL    | ELECTRICAL TECHNICIAN                        | 2,826.18    |
| PW ELECTRICAL    | LEAD ELECTRICAL TECHNICIAN                   | 1,432.92    |
| PW ELECTRICAL    | LEAD PUBLIC WORKS MAINT WORK                 | 2,304.03    |
| PW ELECTRICAL    | MISC HOURLY - PW SIGNALS                     | 90.00       |
| PW ELECTRICAL    | SR ELECTRICAL TECHNICIAN                     | 1,217.71    |
| PW ELECTRICAL    | SR PUBLIC WORKS MAINT WORKER                 | 1,921.67    |
| PW ENGINEERING   | ADMINISTRATIVE ASSISTANT I                   | 6,778.73    |
| PW ENGINEERING   | ASSOC CIVIL ENGINEER                         | 8,461.88    |
| PW ENGINEERING   | ASSOC CIVIL ENGINEER                         | 10,536.32   |
| PW ENGINEERING   | ASST ENGINEER                                | 4,054.05    |
| PW ENGINEERING   | CITY ENGINEER                                | 18,354.60   |
| PW ENGINEERING   | ENGINEERING TECHNICIAN                       | 13,569.34   |
| PW ENGINEERING   | OFFICE SPECIALIST                            | 3,042.54    |
| PW ENGINEERING   | PUBLIC WORKS INSPECTOR                       | 989.46      |
| PW ENGINEERING   | PUBLIC WORKS INSPECTOR                       | 26,174.64   |
| PW ENGINEERING   | SR CIVIL ENGINEER                            | 12,980.28   |
| PW ENGINEERING   | SR CIVIL ENGINEER                            | 37,434.24   |
| PW SEWER MAINT   | LEAD PUBLIC WORKS MAINT WORK                 | 604.11      |
| PW SEWER MAINT   | LEAD PUBLIC WORKS MAINT WORK                 | 4,480.06    |
| PW SEWER MAINT   | PUBLIC WORKS MAINT WORKER                    | 1,193.40    |
| PW SEWER MAINT   | PUBLIC WORKS MAINT WORKER                    | 1,505.55    |
| PW SEWER MAINT   | PUBLIC WORKS MAINT WORKER                    | 7,511.03    |
| PW SEWER STORM   | PUBLIC WORKS MAINT WORKER                    | 3,880.10    |
| PW STREETS       | EQUIPMENT OPERATOR                           | 1,492.60    |
| PW STREETS       | EQUIPMENT OPERATOR                           | 11,573.49   |
| PW STREETS       | LEAD PUBLIC WORKS MAINT WORK                 | 2,144.03    |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 24,456.28   |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 27,665.77   |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 3,623.52    |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 663.33      |
| PW STREETS       | PUBLIC WORKS MAINT WORKER                    | 8,093.55    |
| PW STREETS       | SR PUBLIC WORKS MAINT WORKER                 | 7,197.46    |
| PW STREETS       | SR PUBLIC WORKS MAINT WORKER                 | 5,123.79    |
| PW STREETS       | SWEEPER OPERATOR                             | 1,961.10    |
| REC BLDG MAINT   | BLDG MAINT CRAFTSWORKER                      | 114.44      |
| REC BLDG MAINT   | BLDG MAINT CRAFTSWORKER                      | 64.03       |
| REC BLDG MAINT   | SR BLDG MAINT CUSTODIAN                      | 24.21       |
| REC PARKS        | MISC HOURLY - PARKS                          | 1,120.00    |
| REC PARKS        | PARK MAINT WORKER                            | 4,316.60    |
| REC PARKS        | PARK MAINT WORKER                            | 17,542.80   |
| REC PARKS        | PARK MAINT WORKER                            | 4,316.60    |
| REC SENIORS      | REC LEADER III                               | 834.80      |
| REC SENIORS      | REC LEADER III                               | 51.52       |

**Totals 2009 1,176,998.97**

Est. FTE 13.66

**OVERSIGHT BOARD 4-3-12 Q & A**

| Row | Description                          | Question   | Answer  |
|-----|--------------------------------------|--|---|
| 59  | Maint. Of Property                   | Please provide additional detail on what these expenses are expected to be.  | therefore higher due to the results of these findings/this service. Staff believes it is fair that the costs incurred in obtaining those higher revenues should therefore be allowed as expenses that are not absorbed into general administration.   |
| 60  | Maint of Property Soft Project costs | Please provide additional detail on what these expenses are expected to be.  | See attachment 59 Cost breakdown. Note that these are conservative estimates based on past usage and 6-month cost will be based on actual use.  |
| 67  | Disp of Property                     | Can this go under the Successor Agency's admin allowance?  | See attachment 60 Cost breakdown. Note that these are conservative estimates and 6-month costs will be based on actual staff time needed.   |
| 68  | Disp of Property soft project costs  | Can this go under the Successor Agency's admin allowance?  | See attachment 67 Cost breakdown. Note that these are conservative estimates and 6-month cost will be based on actual use.  |
| 71  | PERS Pension Obligations             | <p>a) Are these costs enforceable obligations?</p> <p>b. How was the accrued obligation for Pension (CalPERS) obligations for RDA funded positions calculated?</p> | <p>Response will be distributed on Monday</p> <p>As the Board may recall, staff estimated this cost, and has asked an outside actuary to do a more refined calculation. That calculation is not yet available. Staff fully expects that the actuary will change the estimate, but staff wanted to have an estimate in the ROPS as a placeholder.</p> <p>Staff did this calculation in two steps. CalPERS reports the total unfunded pension obligation to employers on an annual basis. First, staff took that total unfunded pension obligation and derived an average per employee. However, because CalPERS spreads the unfunded liability cost over a 30 year timeframe, staff prorated the result of the first calculation based on the number of years since the City granted enhanced retirement benefits (11) until the current year to get a ratio to estimate the costs incurred to date. The result (11/30) was as proration of 36.7% of the total unfunded pension liability per employee. These calculations were made separately for Safety employees and for non-Safety employees and the results were \$876,000. Again, this is an estimate at this time.</p> |
| 72  | Retiree Health Obligations           | How was the accrued obligation for retiree health obligations for RDA funded positions calculated?   | As the Board may recall, staff estimated this cost, and has asked an outside actuary to do a more refined calculation. That calculation is not yet available. Staff fully expects that the actuary will change the estimate, but staff wanted to have an estimate in the  |



# Redevelopment Successor Agency Oversight Board Staff Report

**DATE:** December 11, 2012

**TO:** Members of the Oversight Board

**FROM:** Marty Van Duyn, Assistant City Manager

**SUBJECT:** APPROVAL OF A LEASE AGREEMENT ALLOWING RED CARPET MARKET INC., DBA PET CLUB STORES TO USE 1 CHESTNUT AVENUE FOR A RETAIL STORE

## RECOMMENDATION

**It is recommended that the Oversight Board adopt a Resolution to approve a Lease Agreement with Red Carpet Market Inc., dba Pet Club Stores to use the building, and the surface parking area, at 1 Chestnut Avenue for a retail store.**

## BACKGROUND

Red Carpet Market Inc., dba Pet Club Stores ("Pet Club") is requesting that the Successor Agency and the Oversight Board approve a Lease Agreement to use the building, and the surface parking lot at 1 Chestnut Avenue as a retail store.

During the May 2012 meeting of the Oversight Board, the realtor representing the Pet Club at the Westborough Plaza requested that the Board consider leasing the building at 1 Chestnut Avenue to his client. The Pet Club has decided to not extend its current lease at Westborough Plaza and would like to continue to do business in South San Francisco. The property at 1 Chestnut Avenue is 1.68-acres and includes a 27,792-square foot building with approximately 110 parking spaces. The building has been used as an auto dealership since the 1970s. During the late 1990s, the building was renovated. However, the building does not comply with current building codes, such as the American Disability Act (ADA) standards. On June 12, the Oversight Board approved the lease criteria to accept bids from potential retailers for a short-term, three-year lease, which would include "no first right of refusal" and a "termination" clause. Following the 30-day open bid advertisement period ending on August 19, Successor Agency staff received one bid, from the Pet Club, to lease the property as a retail store. Agency staff reviewed the proposal for consistency with the approved lease criteria and prepared a counter proposal. On October 3, 2012, the Pet Club's submitted an amendment to the proposal, which was presented to Oversight Board in October (see attachment 3). Subsequent to Boards review of the amended proposal and staff's counter proposal, Agency staff and the Pet Club negotiated a Lease Agreement.

## DISCUSSION

Successor Agency staff and the representative for the Pet Club have negotiated a Lease Agreement

that complies with the approved lease criteria and is consistent with the terms of the proposal presented to the Successor Agency and Oversight Board in October 2012. The key components of the Agreement include the following:

- A three-year lease term with the possibility of a single one-year extension. If the tenant elects to extend the Lease, the tenant shall not receive any set up allowance.
- The tenant shall receive a set up allowance up to \$500,000 to undertake the necessary tenant improvements. The tenant shall show evidence of completing setup work as a condition of receiving credit.
- The Lease Agreement includes a “Work Plan” that specifies that the tenant shall apply for all required permits and outlines how the allowance will be applied to the rent.
- The tenant shall vacate the site at the end of the lease term.
- The tenant would not receive relocation credits or have a right of first refusal.
- The Tenant would be responsible for utilities and maintenance in the building and on the site (The City would be responsible for underground utilities between the building and the street connection).
- The City will deliver building in “as is” condition (HVAC, water and sewer shall be in working order).
- The Successor Agency has the right sell the property during the lease term.
- The Lease Agreement may be terminated prior to the end of the lease term if the tenant fails to comply with the provisions of the Agreement.

**Rent Structure**

|   | <b>Lease Agreement</b>   |
|---|--|
| <b>Proposed Lease Area and Gross Rent</b> | \$37,519/month, based on a rental rate of \$1.35 per square feet in a 27,792 sf. Building<br>\$450,228/year<br>\$1,350,684/ 3-years  |
| <b>Set Up Allowance</b>                   | \$500,000 or \$13,889/month over 36 months for the initial Lease term. Tenant shall show evidence of completing set up work prior to occupancy as a condition of receiving credit. The allowance will apply only to actual costs for tenant improvement work undertaken prior to occupancy. The tenant will not receive an allowance for the one-year lease extension. |
| <b>Net Rent</b>                           | \$23,630/month<br>\$283,560/year<br>\$850,680/3-years  |

**Successor Agency**

The proposed Lease Agreement would be presented to the Successor Agency during the public meeting on December 10, 2012. Staff will report the Successor Agency discussion and recommendation during the Oversight Board meeting.

**CONCLUSION**

Following an official 30-day open bid period in July and August 2012, the Successor Agency and the Oversight Board received a proposal from the Pet Club to lease the property at 1 Chestnut Avenue for a retail use. Successor Agency evaluated the Pet Club's proposal to determine if it meets the leasing criteria listed above and, following the Oversight Board's direction, negotiated a Lease Agreement with the Pet Club's representative. It is recommended that the Oversight Board adopt a Resolution approving the proposed lease for the property at 1 Chestnut Avenue.

By:   
Marty Van Duyn  
Assistant City Manager and Director

Approved:  -   
Barry M. Nagel  
City Manager

Attachments:

- 1. Resolution
- 2. Lease Agreement, with Exhibits
- 3. Proposal from Victor M. Catanzaro, October 3, 2012
- 4. Letter from Victor M. Catanzaro, October 9, 2012

RESOLUTION NO. \_\_\_\_

OVERSIGHT BOARD FOR THE SUCCESSOR AGENCY TO THE  
REDEVELOPMENT AGENCY OF THE CITY OF SOUTH SAN FRANCISCO

RESOLUTION APPROVING A LEASE AGREEMENT WITH  
RED CART MARKET INC. DBA PET CLUB STORES, A  
CALIFORNIA CORPORATION, FOR 1 CHESTNUT AVENUE  
IN SOUTH SAN FRANCISCO

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WHEREAS, on May 2, 2011, the City of South San Francisco (“City”) acquired that certain real property located at 1 Chestnut Avenue in South San Francisco, California (“Property”) from the Redevelopment Agency of the City of South San Francisco (“Agency”). Pursuant to Health and Safety Code Section 34167.5, the State Controller may deem such transfer to have been unauthorized, resulting instead to a transfer to the Successor Agency by operation of law. In any event, the City will likely convey the Property to the Successor Agency if necessary; and

WHEREAS, pursuant to City Council Resolution No. 08-2012, adopted January 25, 2012, the City affirmed its agreement to serve as the Successor Agency to the Agency, pursuant to Health and Safety Code Section 34173; and

WHEREAS, pursuant to City Council Resolution No. \_\_\_\_-2012, adopted \_\_\_\_\_, 2012, in accordance with Health and Safety Code Section 34173(g), as added by Assembly Bill 1484, the City established the Successor Agency as an entity separate and distinct from the City; and

WHEREAS, on October 10, 2012, Pet Club submitted a letter to the Successor Agency and the Oversight Board requesting that the Successor Agency and the Oversight Board approve a Lease Agreement for the entire building and site at 1 Chestnut Avenue for a retail use; and

WHEREAS, during two closed session meetings with the Successor Agency and the Oversight Board in October and November 2012, City staff presented the proposal and received authorization to negotiate a Lease Agreement with the Pet Club; and

WHEREAS, Staff and Pet Club’s representative have negotiated a Lease Agreement that is consistent with the Successor Agency and Oversight Boards direction; and

WHEREAS, the Successor Agency has adopted a Resolution approving the Lease Agreement and authorizing its execution, and recommending that the Oversight Board approve the Lease Agreement; and

WHEREAS, the Oversight Board has considered the terms of the proposed Lease Agreement, which is for a term of three years, with a one-year option for extension, at a duly-noticed public meeting; and

WHEREAS, Health and Safety Code Section 34179(e) requires that all actions taken by the Oversight Board shall be adopted by resolution.

NOW, THEREFORE, the Oversight Board does hereby resolve as follows:

1. The Recitals set forth above are true and correct, and are incorporated herein by reference.
2. The Lease Agreement between the Successor Agency and Red Cart Market Inc., dba Pet Club Stores for 1 Chestnut Avenue, in the form on file with the City Clerk, is hereby approved.
3. Staff is directed to transmit this Resolution and the Lease Agreement, and related information to the State Department of Finance in accordance with Assembly Bill x1 26, as modified by Assembly Bill 1484.

\* \* \* \* \*

I hereby certify that the foregoing Resolution was regularly introduced and adopted by the Oversight Board for the Successor Agency to the Redevelopment Agency of the City of South San Francisco at a meeting held on the \_\_\_\_\_ day of December, 2012 by the following vote:

AYES: \_\_\_\_\_

NOES: \_\_\_\_\_

ABSTAIN: \_\_\_\_\_

ABSENT: \_\_\_\_\_

ATTEST: \_\_\_\_\_  
City Clerk

**LEASE AGREEMENT  
(One Chestnut Avenue)**

This Lease Agreement (“Lease”) is entered into effective as of \_\_\_\_\_, 2012 (the “Effective Date”) by and between the SUCCESSOR AGENCY TO THE REDEVELOPMENT AGENCY OF THE CITY OF SOUTH SAN FRANCISCO, a public entity, (“Landlord” or “Agency”), and RED CART MARKET INC. dba PET CLUB STORES, a California Corporation (“Tenant”). Landlord and Tenant are hereinafter referred to collectively as the “Parties.”

**ARTICLE I**

**BASIC LEASE PROVISIONS**

- 1.1 **Landlord’s mailing address:** City of South San Francisco, P.O. Box 711, South San Francisco, CA 94083
- 1.2 **Landlord’s contact:** Barry M. Nagel, Executive Director. Telephone: (650) 877-8500.
- 1.3 **Tenant’s address:** Pet Club, 3535 Hollis Street, Emeryville, CA 94608, Telephone: (510) 595-8120

with copy to:

Wall Street Properties, Commercial Real Estate, 922 S. Claremont Street, San Mateo, CA 94402, Telephone: (650) 401-8500

- 1.4 **Tenant’s contact:** Tom Lee
- 1.5 **Premises address:** 1 Chestnut Avenue, South San Francisco, CA 94080.

1.6 **Premises Square Footage and Location:**

**Rentable Square Footage:** 27,792 square feet

**Usable Square Footage:** 27,792 square feet

Premises are depicted in Exhibit A.

- 1.7 **Commencement Date:** \_\_\_\_\_, 2013 [90 days after execution by both Parties following City/Successor Agency approval and Successor Agency Oversight Board (“Oversight Board”) adoption of a resolution], plus (a) expiration of the statutory review period for the California Department of Finance (“DOF”) pursuant to

Health and Safety Code Section 34181 (h); or (b) expiration of the statutory review period pursuant to Health and Safety Code Section 34181 (f), if so extended by DOF; or (c) the date upon which DOF issues written approval of the Oversight Board action. Issuance of building permits shall also be a condition of Commencement. Tenant shall cause a complete building permit application together with required supporting documents and architectural plans to be submitted to the City building division within ten (10) business days from Oversight Board approval of the Lease.

1.8 **Term:** Thirty-six (36) months.

1.9 **Expiration Date:** \_\_\_\_\_, 2016

1.10 **Option(s) to Extend Term:** One (1) option to extend the Term for a period of twelve (12) months. See Section 3.5.

1.11 **Base Rent:**

| <b>Period</b>                 | <b>Monthly Base Rent</b> | <b>Annual Base Rent</b> | <b>Base Rent Per Rentable Square Foot</b> |
|-------------------------------|--------------------------|-------------------------|---|
| First Year<br>(months 1-12)   | \$37,519.00              | \$450,228.00            | \$1.35                                    |
| Second Year<br>(months 13-24) | \$37,519.00              | \$450,228.00            | \$1.35                                    |
| Third Year<br>(months 25-36)  | \$37,519.00              | \$450,228.00            | \$1.35                                    |

1.12 **Security Deposit:** Upon execution hereof Tenant shall deposit with Landlord the sum of \$37,519.00, as security for the full and faithful performance of each and every term, provision, covenant and condition of this Lease, as set forth in Section 4.6.

1.13 **Permitted Uses:** Retail store with veterinarian, clinic, pet grooming and washing, and pet adoption services, only in accordance with Applicable Laws.

1.14 **Parking:** Tenant may use up to one hundred forty-one (141) parking spaces in Landlord's surface parking lot on an unreserved basis.

1.15 **Tenant Improvement Allowance:** Five Hundred Thousand Dollars (\$500,000.00) amortized over the three-year term or Thirteen Thousand Eight Hundred Eighty-Nine Dollars (\$13,889.00) per month. The annual net rental will be Two Hundred Eighty-Three Thousand Five Hundred Sixty Dollars (\$283,560.00) and the monthly Net Rent will be Twenty-Three Thousand Six Hundred and Thirty Dollars (\$23,630.00). Net Rent over the thirty-six (36) month term will be Eight Hundred Fifty Thousand Six Hundred Eighty Dollars

(\$850,680). The Tenant Improvement Allowance is further described in Section 17.2 and Exhibit B to this Lease.

1.16 **Net Rent:**

| <b>Period</b>                   | <b>Monthly<br/>Base Rent</b> | <b>TI<br/>Allowance</b> | <b>Net Rent</b> |
|---------------------------------|------------------------------|-------------------------|-----------------|
| First Year<br>(months 1 - 12)   | \$37,519.00                  | (\$13,889.00)           | \$23,630.00     |
| Second Year<br>(months 13 - 24) | \$37,519.00                  | (\$13,889.00)           | \$23,630.00     |
| Third Year<br>(months 25 - 36)  | \$37,519.00                  | (\$13,889.00)           | \$23,630.00     |

## ARTICLE II

### DEFINITIONS

Definitions. As used in this Lease, the following terms shall have the definitions set forth below. Additional terms are defined in the remainder of the Lease.

2.1 “**Additional Rent**” means any and all sums other than Base Rent which Tenant is or becomes obligated to pay to Landlord under this Lease (whether or not specifically called “Additional Rent” in this Lease).

2.2 “**Affiliate of Tenant**” means any entity that controls, is controlled by, or is under common control with Tenant. “**Control**” means the direct or indirect ownership of more than fifty percent (50%) of the voting securities of an entity or possession of the right to vote more than fifty percent (50%) of the voting interest in the ordinary direction of the entity’s affairs.

2.3 “**Alterations**” means any alterations, decorations, modifications, additions or improvements made in, on, about, under or contiguous to the Premises by or for the benefit of Tenant (other than the Tenant Improvements) including but not limited to, telecommunications and/or data cabling, lighting, HVAC and electrical fixtures, pipes and conduits, partitions, cabinetwork and carpeting.

2.4 “**Applicable Laws**” is defined in Section 5.3.

2.5 “**Base Rent**” means for each Lease Year the monthly amount payable per rentable square foot of the Premises set forth in Section 1.11.

2.6 “**Building**” means the building located at One Chestnut Avenue, South San Francisco, California.

2.7 “**Claims**” is defined in Section 6.3.

2.8 “**Commencement Date**” is the date set forth in Section 1.7.

2.9 “**Common Area**” means all areas and facilities located on the Land **excepting** therefrom the Building. The Common Area includes, but is not limited to, parking areas, access and perimeter roads, sidewalks, landscaped areas and similar areas and facilities.

2.10 “**Environmental Laws**” is defined in Section 6.6.

2.11 “**Hazardous Material**” is defined in Section 6.5.

2.12 “**Indemnitees**” is defined in Section 6.3.

2.13 “**Net Rent**” means for each Lease Year the monthly amount payable per rentable square foot of the Premises as Base Rent, after application of the monthly Tenant Improvement Allowance set forth in Section 1.16.

2.14 “**Premises**” means the premises shown on Exhibit A consisting of 27,792 square feet of rentable space in the Building.

2.15 “**Real Property**” means collectively, (i) the Building; (ii) the parcel of real property on which the Building is situated (the “**Land**”); and (iii) the other improvements on the Land, including, without limitation, a parking lot, driveways, lighting and landscaping.

2.16 “**Real Property Taxes**” is defined in Section 4.5.

2.17 “**Rent**” means Base Rent and Additional Rent, collectively.

2.18 “**Tenant Improvements**” means those certain improvements to be constructed on the Premises as provided in Section 17.2 and Exhibit B.

2.19 “**Tenant Parties**” is defined in Section 6.1.

2.20 “**Term**” means the term of this Lease as set forth in Section 1.8 as such may be extended pursuant to the terms hereof.

### ARTICLE III

## PREMISES AND TERM

3.1 **Lease of Premises.** Subject to and upon the terms and conditions set forth herein, Landlord hereby leases the Real Property to Tenant and Tenant hereby leases the Real Property from Landlord. A portion of the Real Property includes the Premises which consist of the Building commonly known as One Chestnut Avenue which is depicted in the diagram attached hereto as Exhibit A. Tenant acknowledges that Landlord has made no representation or warranty regarding the condition of the Premises, the Building or the Real Property except as specifically stated in this Lease.

As used in this Lease, the term “**Rentable Square Footage**” means the net rentable area measured according to standards similar to the standards published by the Building Owners and Managers Association International, Publication ANSI Z65.1-1996, as amended from time to time. The Parties agree that the Rentable Square Footage of the Premises is 27,792 square feet and the Usable Square Footage of the Premises is also 27,792 square feet. Tenant and Landlord hereby stipulate and agree that same are correct, notwithstanding any minor variations in measurement or other minor variations that may have been incurred in the calculation thereof. If the Building is ever demolished, altered, remodeled, renovated, expanded or otherwise changed in such a manner as to alter the amount of space contained therein, then the Rentable Square Footage of the Building shall be adjusted and recalculated by using the foregoing method of determining Rentable Square Footage, but such recalculation shall not increase the rental hereunder. The Rentable Square Footage of the Building is stipulated for all purposes to be 27,792 square feet.

3.2 **Term and Commencement.** The Term of this Lease shall commence on the Commencement Date, and unless sooner terminated as provided herein, the Term shall be for the period set forth in Section 1.8 as the same may be extended in accordance with any option to extend the Term granted herein.

3.3 **Delay in Delivery of Premises.** If Landlord fails to deliver possession of the Real Property to Tenant on or before the Commencement Date, Landlord shall not be subject to any liability for its failure to do so. This failure shall not affect the validity of this Lease or the obligations of Tenant hereunder, but the Lease Term shall commence on the date upon which Landlord delivers possession of the Real Property to Tenant.

3.4 **Early Access.** Tenant shall not occupy the Real Property prior to the Commencement Date except with the express prior written consent of Landlord. Provided that (i) the Lease has been executed by Tenant and Landlord; (ii) Tenant has provided to Landlord certificates of insurance for all insurance that Tenant is required to maintain under this Lease, the Security Deposit, and the amount of first month's Rent; and (iii) such access does not interfere with the work of Landlord, including without limitation, as applicable, any work of Landlord pursuant to Exhibit B, or any work of another tenant; Tenant shall be permitted to access to the Real Property commencing upon full execution of this Lease, and thus prior to the Commencement Date, for the purpose of installing Tenant's designated trade fixtures and other necessary improvements and to conduct such work as may be necessary to obtain necessary

permits. Such early access shall not be for the purpose of operating Tenant's business on the Real Property. Prior to the Commencement Date, all of the terms and provisions of this Lease shall apply to Tenant's use of the Real Property except for the requirement for the payment of Rent beyond that provided for in this Section 3.4, and Tenant shall abide by all of such terms and provisions. Notwithstanding the foregoing, Tenant acknowledges that in no event shall early access be available until this Lease has been approved by Resolution of the Oversight Board, and the time for review of such Oversight Board action by the California Department of Finance ("DOF") has expired without challenge from or disapproval by DOF or alternatively the Lease is approved by DOF before expiration of the DOF review period, whichever is the earlier to occur.

**3.5 Option to Extend Term.** Landlord grants Tenant one option to extend the Lease Term ("**Extension Option**") for a period of twelve (12) months ("**Extension Term**"), subject to the conditions set forth in this Section 3.5. Tenant shall have no other right to extend the Term beyond the Extension Term.

**3.5.1 Extension Option Conditions.** The Extension Option may be exercised with respect to all or any portion of the Real Property subject to this Lease at the time of exercise only by written notice delivered by Tenant to Landlord no later than **six (6)** months prior to the expiration of the initial Term, and only if as of the date of delivery of the notice, Tenant is not in default under this Lease. The Extension Option may be exercised only by the originally named Tenant or by an assignee or sublessee approved pursuant to Article X and only if the originally named Tenant or such approved assignee or sublessee is not in default under the Lease at the time of delivery of notice of exercise and occupies the entire Premises as of the date it exercises the Extension Option. If Tenant or such approved assignee or sublessee properly exercises the Extension Option and is not in default at the end of the initial Lease Term, the Term shall be extended for the Extension Term. The failure to exercise the Extension Option in accordance with this Section shall constitute an election to terminate this Lease at the end of the initial Term, and Landlord's acceptance of any Rent subsequent to the expiration of such Term shall not constitute a waiver by Landlord of the requirement of timely exercise of the Extension Option by delivery of notice pursuant to this Section.

**3.5.2 Extension Term Rent.** The Rent payable by Tenant at the commencement of and during the Extension Term shall be equal to the Fair Market Rental Value, and if the Parties cannot reach agreement within sixty (60) days of the notice of election to extend as provided in Section 3.5.1, the Fair Market Rental Value shall be established in the manner set forth in Section 3.5.3, below. For purposes of this Section, "**Fair Market Rental Value**" shall be the amount that a willing, comparable, new (i.e., non-renewal), non-equity tenant would pay, and that a willing landlord of a comparable space in the vicinity of the Building would accept at arms' length. Appropriate consideration shall be given to: (i) the annual rental rate per rentable square foot; (ii) the definition of rentable square feet for purposes of comparing the rate; (iii) location and quality of the Building; (iv) the financial condition (e.g., creditworthiness) of Tenant; (v) escalation (including type, base year and stop) and abatement provisions (if any) reflecting free rent and/or no rent during the period of construction; (vi) brokerage

commissions, if any, (vii) length of the lease term; (viii) size of the Premises; (ix) building standard work letter and/or tenant improvement allowance, if any; provided, however, the Fair Market Rental Value shall not include any tenant improvements or any alterations made by Tenant at Tenant's expense; (x) condition of space; (xi) lease takeover / assumptions; (xii) moving expenses and other concessions (if any); (xiii) extent of services to be provided; (xiv) distinctions between "gross" and "net" leases; (xv) base year figures or expense stops (if any) for escalation purposes for both operating costs and ad valorem / real estate taxes; (xvi) the time the particular rental rate under consideration becomes or is to become effective; (xvii) applicable caps (if any) on the amount of real estate taxes and assessments passed through to tenants; and (xviii) other generally applicable conditions of tenancy for the space in question.

**3.5.3 Arbitration.** If Landlord and Tenant are not able to agree on the Fair Market Rental Value of the Premises within sixty (60) days following the date upon which Tenant delivers notice of exercise of the Extension Option (the "**Agreement Deadline**"), the Fair Market Rental Value will be determined by "baseball arbitration" in accordance with this Section 3.5.3. Landlord and Tenant shall each make a separate determination of Fair Market Rental Value and notify the other Party within fifteen (15) days following after the Agreement Deadline. If either Party fails to make a determination of the Fair Market Rental Value within the fifteen (15) day period, that failure shall be conclusively deemed to be that Party's approval of the Fair Market Rental Value submitted within such period by the other Party. If both Parties timely make determinations of Fair Market Rental Value, such determinations shall be submitted to an arbitrator. The determination of the arbitrator shall be limited to the sole issue of determining which of the Party's determinations is closest to the actual Fair Market Rental Value as determined by the arbitrator, taking into consideration the requirements of Section 3.5.2. The arbitrator must be a licensed real estate broker who has been active in the leasing of commercial properties in the South San Francisco area over the immediately prior five-year period. If the Parties are unable to agree upon an arbitrator, then each Party shall appoint one arbitrator within fifteen (15) days following the Agreement Deadline and shall notify the other Party of such appointment. Within ten (10) days following the appointment of the second arbitrator, the two arbitrators so selected shall agree upon and appoint a third arbitrator who shall have the qualifications specified in this paragraph and shall notify the Parties of such appointment. Within thirty (30) days following the appointment of the third arbitrator, the three arbitrators shall decide whether to use Landlord's or Tenant's determination of Fair Market Rental Value and shall notify the Parties of their decision. The decision of the majority of the arbitrators shall be binding. If either Party fails to appoint an arbitrator within fifteen (15) days following the Agreement Deadline, then the arbitrator timely appointed shall reach a decision and shall notify Landlord and Tenant of such decision within thirty (30) days after such arbitrator's appointment. The decision of such arbitrator or arbitrators, as applicable, shall be binding on Landlord and Tenant. The cost of the arbitration shall be paid by the losing Party.

**3.5.4 Amendment to Lease.** If Tenant timely exercises the Extension Option, Landlord and Tenant shall, within fifteen (15) days after the Extension Term rent

is determined, execute an amendment to this Lease extending the Term on the terms and conditions of Rent as set forth in Section 3.5.

3.6 **No Representations.** Tenant acknowledges that neither Landlord nor any of Landlord's agents has made any representation or warranty as to the suitability or fitness of the Premises for the conduct of Tenant's business, and that neither Landlord nor any of Landlord's agents has agreed to undertake any alterations or additions or to construct any tenant improvements to the Premises except as expressly provided in this Lease.

3.7 **AS-IS Lease.** Notwithstanding that Tenant Improvements will be made pursuant to this Lease, Tenant acknowledges and agrees that by executing this Lease Tenant shall be deemed to have approved of all characteristics and conditions of the Premises, the Building and the Real Property, following its own independent investigation and due diligence, and that Tenant is leasing and accepting same in its present condition, "AS IS" WHERE IS AND WITH ALL FAULTS, and no present or latent defect or deficiency in any legal or physical condition thereof, whether or not known or discovered, shall affect the rights of either Landlord or Tenant hereunder, nor shall Rent be reduced as a consequence thereof. Without limiting the foregoing, Landlord shall, prior to the Commencement Date, ensure that the Building's mechanical equipment, plumbing and roof are in working order. Except as expressly provided herein, Landlord shall have no further obligation to make the Building ready for Tenant. Without limiting the foregoing, Landlord and Tenant acknowledge that Landlord shall have no obligation to remove or pay for the removal of flooring and mastic. Notwithstanding the provisions of this Section 3.7, the Parties acknowledge and agree that Tenant shall have no liability for Hazardous Substances, if any, which exist and are present on the Real Property as of the Effective Date of the Lease; provided, however, that Tenant shall have the duty of establishing the date of any release of Hazardous Substances for which it claims no responsibility.

3.8 **No Right of First Refusal.** Nothing contained herein, including without limitation the provisions of Section 3.5 regarding Tenant's conditional option to extend the Term hereof, is or shall be deemed to constitute a right of first refusal to purchase the Property from Landlord or to require Landlord to sell the Property to Tenant, or any other preemptive right in favor of Tenant.

## ARTICLE IV

### RENT, OPERATING EXPENSES, TAXES AND SECURITY DEPOSIT

4.1 **Monthly Rent.** From and after the Commencement Date, Tenant shall pay to Landlord for each calendar month of the Term, the monthly Base Rent set forth in Section 1.11, as the same may be adjusted upon Tenant's exercise of the Extension Option as provided in Section 3.5.2. Each monthly installment of Base Rent shall be due and payable to Landlord in lawful money of the United States, in advance, on the first (1st) day of each calendar month during the Term, subject to the provisions of Sections

1.15 and 17.2, without abatement, deduction, claim or offset, and without prior notice, invoice or demand, at Landlord's address set forth in Section 1.1 or such other place as Landlord may designate from time to time. Tenant's payment of Base Rent for the first month of the Term shall be delivered to Landlord concurrently with Tenant's execution of this Lease.

4.2 **Prorations.** Monthly installments for any fractional calendar month at the beginning or end of the Term shall be prorated based on the number of days in such month.

4.3 **Additional Rent; Triple Net Lease.** All Additional Rent, including without limitation, all of Tenant's required payments pursuant to this Article IV, shall be due and payable to Landlord in lawful money of the United States subject to the provisions of Sections 1.15 and 17.2, without abatement, deduction, claim or offset within twenty (20) days of receipt of Landlord's invoice or statement for same (or if this Lease provides another time for the payment of certain items of Additional Rent, then at such other time) at Landlord's address set forth in Section 1.1 or such other place as Landlord may designate from time to time. This is a triple net lease to Landlord. Tenant agrees to pay, without abatement, deduction, claim or offset, all costs and expenses relating to the Premises or any part thereof, of any kind or nature whatsoever. Such costs and expenses shall include, without limitation, all amounts attributable to, paid or incurred in connection with the operation, repair, restoration, maintenance and management of the Premises; property taxes (subject to limitation of real estate taxes contained in Section 4.5.3, below) and payments in lieu thereof; rent taxes; gross receipt taxes (whether assessed against Landlord or assessed against Tenant and collected by Landlord, or both); water and sewer charges; insurance premiums (excluding flood and earthquake); utilities; refuse disposal; lighting (including outside lighting); fire-detection systems including monitoring, maintenance and repair; security; janitorial services; labor; air conditioning and heating; maintenance and repair costs and service contracts; costs of licenses, permits and inspections; and all other costs and expenses paid or incurred with respect to the Premises or part thereof.

4.4 **Late Charge.** Tenant acknowledges that the late payment of Rent will cause Landlord to incur administrative costs and other damages, the exact amount of which would be impracticable or extremely difficult to ascertain. Landlord and Tenant agree that if Landlord does not receive any such payment within ten (10) calendar days after such payment is due, Tenant shall pay to Landlord as Additional Rent an amount equal to five percent (5%) of the overdue amount as a late charge for each month or partial month that such amount remains unpaid. The Parties acknowledge that this late charge represents a fair and reasonable estimate of the costs that Landlord will incur by reason of the late payment by Tenant. Acceptance of any late Rent and late charge therefore shall not prevent Landlord from exercising any of the other rights and remedies available to Landlord for any other Event of Default under this Lease.

4.5 **Taxes.** The term "Real Property Taxes" means any form of tax, assessment, charge, license, fee, penalty (if a result of Tenant's delinquency), real

property or other tax (other than Landlord's net income, estate, succession, inheritance, or franchise taxes), now or hereafter imposed with respect to the Building, the Real Property or any part thereof (including any Alterations by any authority having the direct or indirect power to tax, or by any city, county, state or federal government or any improvement district or other district or division thereof, whether such tax or any portion thereof (i) is determined by the area of the Building, the Real Property, or any part thereof, or (ii) is levied or assessed in lieu of, in substitution for, or in addition to, existing or additional taxes with respect to the Building, the Real Property or any part thereof whether or not now customary or within the contemplation of Landlord or Tenant. Tenant and Landlord intend that all Real Property Taxes, including without limitation all new and increased assessments, taxes, possessory interest taxes charged or levied in place of real property taxes, fees, levies, and charges and all similar assessments, taxes, fees, levies and charges shall be included within the definition of "Real Property Taxes" for purposes of this Lease.

**4.5.1 Apportionment of Taxes.** If the Building is assessed as part of a larger parcel, then Landlord shall equitably apportion the Real Property Taxes and reasonably determine the Real Property Taxes attributable to the Building. If other buildings exist on the assessed parcel, the Real Property Taxes apportioned to the Building shall be based upon the ratio of the square footage of the Building to the square footage of all buildings on the assessed parcel. Landlord's reasonable determination of such apportionment shall be conclusive.

**4.5.2 Tax on Improvements.** Notwithstanding anything to the contrary set forth in this Lease, Tenant shall pay (subject to real estate tax limitation as provided in Section 4.5.3, below) prior to delinquency any and all taxes, fees and charges which are levied or assessed against Landlord or Tenant: (a) upon Tenant's equipment, furniture, fixtures, improvements and other personal property located in the Premises, (b) by virtue of any alterations or leasehold improvements made to the Premises by Tenant, and (c) upon this transaction or any document to which Tenant is a party creating or transferring an interest or an estate in the Premises. If any such tax, fee or charge is paid by Landlord, Tenant shall reimburse Landlord for Landlord's payment upon demand.

**4.5.3 Real Property Tax Limitation.** Notwithstanding the provisions of Section 4.5 Tenant's increase of real property tax shall be governed by a maximum adjustment of three percent (3.00%) per annum of the Real Estate Tax due for fiscal year 2012/2013 assessed against the Real Property. Notwithstanding the foregoing, Tenant shall pay all taxes assessed which result from water usage or sewer charge assessment and assessment against Tenant's Improvements described in Section 17.2 and Exhibit B.

Property ownership transfers shall be governed by the same limitation on increases of Tenant's obligation to pay Real Property Taxes as stated above.

**4.6 Security Deposit.** If Tenant fails to pay Rent, or otherwise defaults under the Lease, Landlord may use, apply or retain all or any portion of said Security Deposit for the payment of any amount due Landlord or to reimburse

or compensate Landlord for any liability, expense, loss or damage which Landlord may suffer or incur by reason thereof. If Landlord uses or applies all or any portion of the Security Deposit, Tenant shall within ten (10) days after written request therefore, deposit monies with Landlord sufficient to restore said Security Deposit to the full amount required by this Lease. Landlord shall not be required to keep the Security Deposit separate from its general accounts.

Within fourteen (14) days after the expiration or termination of this Lease, if Landlord elects to apply the Security Deposit only to unpaid Rent, and otherwise within thirty (30) days after the Premises have been vacated pursuant to Article XIV, Landlord shall return that portion of the Security Deposit not used or applied by Landlord. No part of the Security Deposit shall be considered to be held in trust, to bear interest or to be prepayment for any monies to be paid by Tenant under this Lease. Tenant shall have no right to apply the Security Deposit, or any portion thereof, to the last month rent due under this Lease.

If Landlord disposes of its interest in the Premises and the Real Property, Landlord may deliver or credit the Security Deposit to Landlord's successor in interest to the Premises and Real Property, and thereupon Landlord shall be relieved of further responsibility with respect to the Security Deposit.

## ARTICLE V

### USE OF PREMISES

5.1 **Permitted Use; Entitlements.** The Premises shall be used solely for the purposes set forth in Section 1.13 and for no other purpose without the written consent of Landlord, which may be granted or withheld in Landlord's sole discretion. Tenant shall not do or suffer or permit anything to be done in or about the Premises, the Building or the Real Property, nor bring or keep anything therein that would in any way subject Landlord to any liability, increase the premium rate of or affect any fire, casualty, rent or other insurance relating to the Real Property or any of the contents of the Building, or cause a cancellation of, or give rise to any defense by the insurer to any claim under, or conflict with, any policies for such insurance. If any act or omission of Tenant results in any such increase in premium rates, Tenant shall pay to Landlord upon demand the amount of such increase.

Tenant shall bear sole responsibility for obtaining and securing all required permits and other entitlements, pursuant to Applicable Laws, prior to commencing occupancy of the Premises unless Landlord and Tenant agree otherwise in writing, and as approved by the Oversight Board.

5.2 **Signage.** Tenant shall obtain the prior written approval of the Landlord, which approval may be withheld in Landlord's sole discretion, before placing any sign or symbol on doors or windows or elsewhere in or about the Premises so as to be visible

from the public areas or exterior of the Building, or upon any other part of the Building or Real Property, including building directories. Any signs or symbols which have been placed without Landlord's written approval may be removed by Landlord. Upon expiration or termination of this Lease, all signs installed by Tenant shall be removed and any damage resulting therefrom shall be promptly repaired by Tenant, or such removal and repair may be done by Landlord and the cost charged to Tenant as Rent. Tenant shall be provided signage as a part of the Building directory.

Tenant is hereby granted the right to place and maintain in place during the Term of this Lease Tenant's name on the exterior of the Building with lighting. The design of the signage and the lighting shall be subject to Landlord's written approval. Landlord shall determine in its reasonable discretion the position, location and configuration of Tenant's name on the Building. All signs or lettering shall conform in all respects to the sign and/or lettering criteria reasonably established by Landlord. All signage shall comply with regulations promulgated by the City of South San Francisco. The cost of Building signage shall be counted toward the Tenant Improvement Allowance.

5.3 **Compliance with Laws.** Tenant shall procure and maintain all governmental approvals, licenses and permits required for the proper and lawful conduct of Tenant's permitted use of the Premises. Tenant shall throughout the Term comply with and shall not use the Premises, the Building or the Real Property, or suffer or permit anything to be done in or about the same which would in any way conflict with, any of the following (collectively "**Applicable Laws**"): (i) the provisions of all recorded covenants, conditions and restrictions applicable to the Building or the Real Property, or (ii) any federal, state, county, local or other governmental agency rules, regulations, statutes, ordinances, orders, standards, requirements or laws now in force or hereafter enacted, promulgated or issued which are applicable to the Real Property, Premises, the Building, or the use or occupancy thereof, including without limitation building, zoning, and fire codes and regulations.

## ARTICLE VI

### ENVIRONMENTAL MATTERS

6.1 **Use of Hazardous Materials.** Tenant shall not cause or permit any Hazardous Material to be generated, brought onto, used, stored, or disposed of in or about the Premises, the Building or the Real Property by Tenant or Tenant's agents, employees, contractors, subtenants or invitees (collectively "**Tenant Parties**"), except for limited quantities of standard office and janitorial supplies. At Tenant's sole cost and expense, Tenant shall use, store and dispose of all such Hazardous Materials in strict compliance with all Environmental Laws, and shall in all other respects comply with all Environmental Laws.

6.2 **Notice of Release or Investigation.** If during the Lease Term (including any extensions), Tenant becomes aware of (a) any actual or threatened release of any Hazardous Material on, under, or about the Premises, the Building or the Real Property,

or (b) any inquiry, investigation, proceeding, or claim by any government agency or other person regarding the presence of Hazardous Material on, under, or about the Premises, the Building, or the Real Property, Tenant shall give Landlord written notice of the release or investigation within five (5) days after learning of it and shall simultaneously furnish to Landlord copies of any claims, notices of violation, reports, or other writings received by Tenant that concern the release or investigation.

**6.3 Indemnification.** Tenant shall defend (with counsel acceptable to Landlord), indemnify and hold harmless Landlord and Landlord's elected and appointed officers, officials, employees, agents and representatives (collectively, "**Indemnitees**") from and against any and all liabilities, losses, damages, fines, deficiencies, penalties, claims, demands, suits, actions, causes of action, legal or administrative proceedings, judgments, costs and expenses (including without limitation reasonable attorneys' fees and expenses, court costs, expert witness fees and post judgment collection costs) (all of the foregoing, collectively "**Claims**") resulting or arising from or in connection with any release of any Hazardous Material in or about the Premises, the Building or the Real Property by Tenant, or Tenant's agents, assignees, sublessees, contractors, or invitees, or any other violation of any Environmental Law by Tenant, or Tenant's agents, assignees, sublessees, contractors, or invitees. This indemnification includes: (i) losses attributable to diminution in the value of the Premises or the Building, (ii) loss or restriction of use of rentable space in the Building, (iii) adverse effect on the marketing of any space in the Building; and (iv) all other liabilities, obligations, penalties, fines, claims, actions (including remedial or enforcement actions of any kind and administrative or judicial proceedings, orders, or judgments), damages (including consequential and punitive damages), and costs (including attorney, consultant, and expert fees and expenses) resulting from the Tenant Parties release or violation. The indemnity provided in this Section shall not extend to Claims to the extent the same are caused by the gross negligence or willful misconduct of Indemnitees. The provisions of this Section shall survive the expiration or termination of this Lease.

**6.3.1 Landlord's Representations and Warranties.** Landlord represents and warrants that Landlord has received no notice, warning, notice of violation, administrative complaint, judicial complaint, or other written notice alleging that the Building or the Real Property are in violation of any Environmental Laws (defined below) or informing Landlord that the Building or the Real Property is subject to investigation or inquiry concerning Hazardous Materials, nor is Landlord aware of any such violation. In addition, to the best knowledge of Landlord, there is no pending or threatened litigation, administrative proceeding, or other legal or governmental action with respect to the Building or the Real Property in connection with the presence of Hazardous Materials in, on or under the Building or the Real Property. Whenever used in this Agreement, the phrase "to the best knowledge of Landlord" shall mean the actual knowledge of Landlord's Superintendent of Parks and Facilities and Public Works Supervisor, Building Maintenance. Without limiting the foregoing, Landlord and Tenant acknowledge that Landlord shall have no obligation to remove or pay for the removal of flooring and mastic. If, however; Hazardous Substances other than flooring and mastic are determined to be present on the Real Property as of the Effective Date of the Lease,

and remedial action is required in relation to the particular Hazardous Substances because a federal, state, or local government agency is requiring such remedial action, then Tenant shall have no responsibility for the cost of any required or necessary repair, cleanup or detoxification or decontamination of any of the Premises, or the preparation and implementation of any closure, remedial action or other required plans in connection therewith (collectively, "Remediation"); provided, however, that Tenant shall provide without charge to Landlord or the applicable party or parties, unfettered access to the Real Property and the Premises for purposes of such Remediation..

**6.4 Remediation Obligations.** If the presence of any Hazardous Material brought onto the Premises or the Building by Tenant or Tenant's employees, agents, contractors, or invitees results in contamination of the Building, Tenant shall promptly take all necessary actions to remove or remediate such Hazardous Materials, whether or not they are present at concentrations exceeding state or federal maximum concentration or action levels, or any governmental agency has issued a cleanup order, at Tenant's sole expense, to return the Premises and the Building to the condition that existed before the introduction of such Hazardous Material. Tenant shall first obtain Landlord's approval of the proposed removal or remedial action. This provision does not limit the indemnification obligation set forth in Section 6.3.

**6.5 Definition of Hazardous Material.** As used in this Lease, the term "**Hazardous Material**" means any hazardous or toxic substance, material, or waste at any concentration that is or becomes regulated by the United States, the State of California, or any government authority having jurisdiction over the Building. Hazardous Material includes: (a) any "hazardous substance," as that term is defined in the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA) (42 United States Code sections 9601-9675); (b) "hazardous waste," as that term is defined in the Resource Conservation and Recovery Act of 1976 (RCRA) (42 United States Code sections 6901-6992k); (c) any pollutant, contaminant, or hazardous, dangerous, or toxic chemical, material, or substance, within the meaning of any other applicable federal, state, or local law, regulation, ordinance, or requirement (including consent decrees and administrative orders imposing liability or standards of conduct concerning any hazardous, dangerous, or toxic waste, substance, or material, now or hereafter in effect); (d) petroleum products; (e) radioactive material, including any source, special nuclear, or byproduct material as defined in 42 United States Code sections 2011-2297g-4; (f) asbestos in any form or condition; and (g) polychlorinated biphenyls (PCBs) and substances or compounds containing PCBs.

**6.6 Definition of Environmental Laws.** As used in this Lease, the term "**Environmental Laws**" means all federal, state and local laws, ordinances, regulations, rules orders and directives pertaining to Hazardous Materials, including without limitation, the laws, statutes, and regulations cited in the preceding Section 6.5, as any of the foregoing may be amended from time to time.

**6.7 Environmental Reports.** Landlord shall provide to Tenant copies of all studies, reports and investigations concerning the environmental condition of the

Building and the Real Property which were prepared within the past five years and which are in Landlord's possession.

## ARTICLE VII

### UTILITIES AND SERVICES

7.1. **Utility Services.** Tenant shall contract and pay for all utility services ("**Utility Services**"), including, without limitation, the following: (i) electricity for Building lighting and power suitable for Use of the Premises as provided in Section 1.13, above including but not limited to ordinary retail store and veterinary service purposes; (ii) air conditioning and heating; and (iii) water for drinking, lavatory and veterinary service purposes.

7.2 **Maintenance Services and Repairs.** Tenant shall be responsible for all interior and exterior maintenance of the Premises, the Building and the Real Property (collectively, "**Maintenance Services**"), including, without limitation: (i) maintenance of all exterior areas of the Building and the Real Property, including without limitation, lighting and landscaping; (ii) cleaning, painting, maintenance and repair of the Building exterior, (iii) maintenance and repair of the Building mechanical, electrical, HVAC and plumbing equipment and systems (excepting below grade plumbing from the street connection to the building exterior wall foundation) and the Building structural components including the roof, foundation, floors and non-load bearing walls (*excepting therefrom damage caused by natural disaster not including fire or an insured peril and damage to structural components existing as of the commencement date*), (iv) maintenance of all areas of the Building and the Real Property including parking lots, walkways, driveways, fences, utility systems, fire sprinklers, corridors, restrooms, windows; (v) supply of public area lamp replacement, (vi) provision of exterior window washing with reasonable frequency, but in no event less than two (2) times per year; and (vii) provision of janitorial services to the common areas ("**Janitorial Services**"). Without limiting the foregoing, Tenant shall be responsible for janitorial service to the Premises and interior window cleaning.

Tenant shall, at all times during the Term of this Lease and any extension thereof, at Tenant's sole expense, keep the Premises (including all Tenant Improvements, Alterations, fixtures and furnishings) in good order, repair and condition. Subject to Landlord's prior approval and within any reasonable period specified by Landlord, Tenant shall, at Tenant's sole expense, promptly and adequately repair all damage to the Premises and replace or repair all damaged or broken fixtures and other leasehold improvements. If Tenant fails to maintain or keep the Premises in good repair or if such failure results in a nuisance or health or safety risk, at Landlord's option, Landlord may perform any such required maintenance and repairs and within ten days after receipt of Landlord's invoice therefor, Tenant shall pay Landlord's costs incurred in connection with such repairs, plus a percentage of such costs sufficient to reimburse Landlord for all overhead, general conditions, fees and other costs and expenses in connection therewith. Landlord's reimbursement for overhead, general conditions, fees and costs shall be a

percentage of costs incurred by Landlord pursuant to this Section 7.2 which said percentage shall be fixed at ten percent (10.00%) of the costs of repair or maintenance incurred by Landlord.

7.3 **Waiver.** Tenant hereby waives the provisions of Sections 1941 and 1942 of the California Civil Code and any other present or future law permitting repairs by a tenant at the expense of a landlord or termination of a lease by reason of the condition of the leased premises.

7.4 **Compliance with Applicable Laws.** Landlord and Tenant shall each comply with (and shall cause their respective employees, agents and contractors to comply with) all Applicable Laws, including without limitation all Environmental Laws, whenever either Party undertakes any work of construction, alteration or improvement in the Premises or the Building,

## ARTICLE VIII

### ALTERATIONS AND ADDITIONS

8.1 **Alterations and Improvements.** Tenant may not make any improvements, alterations, additions or changes to the Premises (“**Alterations**”) without the prior written approval of Landlord, which approval shall not be unreasonably withheld or delayed. Any such Alterations shall be done at Tenant’s expense, in a good and workmanlike manner conforming in quality and design with the Premises existing as of the Commencement Date, by a licensed contractor reasonably approved by Landlord, in conformity with plans and specifications reviewed and approved by Landlord, and in compliance with all Applicable Laws. Tenant shall obtain all necessary governmental approvals and permits for such Alterations. Tenant shall give Landlord not less than ten (10) business days’ notice prior to the commencement of construction so that Landlord may post a notice of nonresponsibility on the Premises. Notwithstanding any other provisions in this Lease, unless Landlord otherwise agrees in writing, Tenant shall remove, prior to expiration of the Term and at Tenant’s sole cost and expense, any and all wires, cables and related telecommunications devices installed by or on behalf of Tenant, and Landlord may at its option by written notice to Tenant, require that Tenant, upon the expiration or sooner termination of this Lease, at Tenant’s expense, remove any or all other Alterations and return the Premises to its condition as of the Commencement Date, normal wear and tear excepted; provided, however, Tenant shall have no obligation to remove the initial Tenant Improvements constructed pursuant to Exhibit B hereto upon expiration of the Term of this Lease. Notwithstanding the improvements and alternations pursuant to those described in Exhibit B, Tenant shall not make any Alterations that: (i) affect the exterior of the Building, (ii) affect any of the structural portions of the Building, including without limitation, the roof, (iii) diminish the value of the Premises, (iv) result in an increase in the demand for utilities or services that Landlord is required to provide, (v) cause an increase in the premiums for hazard or liability insurance carried by Landlord, or (vi) overload the floor load capacity or unduly burden the plumbing, heating, ventilation, air conditioning, electrical or other basic systems that serve the Building. Upon completion of any Alteration, Tenant shall (a) cause a timely notice of

completion to be recorded in the official records of San Mateo County in accordance with Civil Code Section 3093 or any successor statute, and (b) deliver to Landlord evidence of full payment and unconditional final waivers of all liens for labor, services, or materials.

8.2 **Liens.** Tenant shall not permit any mechanics', materialmen's or other liens, to be filed against the Building or the Real Property or against Tenant's leasehold interest in the Premises. Landlord has the right at all times to post and keep posted on the Premises any notice that it considers necessary for protection from such liens. If Tenant fails to cause the release of record of any lien(s) filed against the Premises or Tenant's leasehold estate therein, by payment or posting of a proper bond within ten (10) days from the date of the lien filing(s), then Landlord may, at Tenant's expense, cause such lien(s) to be released by any means Landlord deems proper, including but not limited to payment of or defense against the claim giving rise to the lien(s). All sums reasonably disbursed, deposited or incurred by Landlord in connection with the release of the lien(s), including but not limited to all costs, expenses and attorney's fees, shall be due and payable by Tenant to Landlord as Additional Rent on demand by Landlord.

## ARTICLE IX

### INSURANCE AND INDEMNITY

9.1 **Indemnity.** To the fullest extent permitted by law, Tenant shall defend (with counsel reasonably acceptable to Landlord), indemnify and hold Indemnitees harmless from and against any and all Claims arising out of or relating directly or indirectly to this Lease or the Premises (including without limitation, Claims for or relating to loss of or damage to property, injury or death of any person or animal), including any Claim arising from or in connection with or in any way attributable to: (i) the use or occupancy, or manner of use or occupancy of the Premises, the Building or the Real Property by Tenant or the Tenant Parties, (ii) any act, error, omission or negligence of Tenant Parties or any invitee, guest or licensee of Tenant in, on or about the Real Property, (iii) any Alterations, (iv) construction of the Tenant Improvements (as defined in Section 1.15 and Section 17.2 ), (v) Tenant's work performed pursuant to Exhibit B hereto, (vi) work performed pursuant to Section 7.2 above, and (vii) any activity, work, or thing done, omitted, permitted, allowed or suffered by Tenant or Tenant Parties in, at, or about the Premises, the Building or the Real Property, except to the extent caused by the gross negligence or willful conduct of Landlord. The provisions of this section shall not be construed or interpreted as in any way restricting, limiting or modifying Tenant's insurance obligations under this Lease. Tenant's compliance with the insurance requirements set forth in this Lease shall not in any way restrict, limit or modify Tenant's indemnification obligations hereunder. The provisions of this section shall survive the expiration or earlier termination of this Lease.

9.2 **Tenant's Insurance.** Tenant shall, at its sole expense, procure and maintain throughout the Term (plus such earlier and later periods as Tenant may be in occupancy of the Premises) all of the following:

(a) Commercial general liability insurance including contractual liability coverage, written on an "occurrence" policy form, covering bodily injury, property damage and personal injury arising out of or relating (directly or indirectly) to Tenant's operations, conduct, assumed liabilities, or use or occupancy of the Premises, the Building or the Real Property naming the Indemnitees as additional insureds, with minimum coverage in the amount of Two Million Dollars (\$2,000,000) per occurrence combined single limit for bodily injury and property damage and Five Million Dollars (\$5,000,000) in the aggregate;

(b) Property insurance protecting Tenant against loss or damage by fire and such other risks as are insurable under then available standard forms of "all risk" insurance policies, covering Tenant's personal property and trade fixtures in or about the Premises or the Real Property, and any improvements and/or Alterations in the Premises, in an amount not less than one hundred percent (100%) of their actual replacement cost or highest insurable value;

(c) Workers' compensation insurance in at least the statutory amounts;  
and

(d) If Tenant operates owned, leased or non-owned vehicles on the Real Property, comprehensive automobile liability insurance with a minimum coverage of one million dollars (\$1,000,000) per occurrence, combined single limit.

The foregoing policies shall protect Tenant as named insured, and Landlord and the other Indemnitees as additional insureds, and if subject to deductibles shall provide for deductible amounts not in excess of those approved in advance in writing by Landlord in its reasonable discretion. Landlord reserves the right to increase the foregoing amount of required liability coverage from time to time (but not more often than once each calendar year) to adequately protect Indemnitees and to require that Tenant cause any of its contractors, vendors or other parties conducting construction, demolition or improvement or remodeling activities or any sub-tenant or sub-lessee in or about the Premises to obtain and maintain insurance as determined by Landlord and as to which the Indemnitees shall be additional insureds.

9.3 **Excess Coverage Liability Policy.** Nothing in this Article IX shall prevent Tenant from obtaining insurance of the kind and in the amounts provided for under this Section under an excess coverage liability insurance policy covering other properties as well as the Premises; provided, however, that any such policy of excess coverage liability insurance (i) shall specify those amounts of the total insurance allocated to the Premises, which amounts shall not be less than the amounts required by Section 9.2, (ii) such amounts so specified shall be sufficient to prevent any one of the insureds from becoming a co-insurer within the terms of the applicable policy, and (iii) shall, as to the Premises, otherwise comply with the requirements of this Article as to endorsements and coverage.

9.3.1 **Self-Insurance.** Any insurance required to be maintained by the Tenant pursuant to this Lease may be maintained under a plan of self-insurance through a wholly-owned subsidiary of Tenant's parent company which specializes in providing such coverage for Tenant's parent company and its subsidiaries, provided that Tenant's parent company's net worth exceeds One Hundred Million Dollars (\$100,000,000). Tenant agrees that if Tenant elects to self-insure, Landlord shall have the same benefits and protections as if Tenant carried insurance with a third-party insurance company satisfying the requirements of this Lease (including without limitation, waive of subrogation provisions).

9.4. **Policy Form.** Each insurance policy required pursuant to Section 9.2 shall be issued by an insurance company licensed in the State of California and with a general policyholders' rating of "A+" or better and a financial size ranking of "Class VIII" or higher in the most recent edition of Best's Insurance Guide. Each insurance policy, other than Tenant's workers' compensation insurance, shall (i) provide that it may not be cancelled or allowed to lapse unless thirty (30) days' prior written notice to Landlord is first given; (ii) provide that no act or omission of Tenant shall affect or limit the obligations of the insurer with respect to any other insured; (iii) include all waiver of subrogation rights endorsement necessary to effect the provisions of Section 9.6; and (iv) provide that the policy and the coverage provided shall be primary, that Landlord, although an additional insured, shall nevertheless be entitled to recovery under such policy for any damage to Landlord or the other Indemnitees by reason of acts or omission of Tenant, and that any coverage carried by Landlord shall be noncontributory with respect to policies carried by Tenant. A certificate evidencing each insurance policy shall be delivered to Landlord by Tenant on or before the Commencement Date, and thereafter Tenant shall deliver to Landlord renewal policies or certificates at least thirty (30) days prior to the expiration dates of expiring policies. If Tenant fails to procure such insurance or to deliver such certificates to Landlord, and such failure continues five (5) business days after notice thereof from Landlord to Tenant, Landlord may, at its option, procure the same for Tenant's account, and the cost thereof shall be paid to Landlord by Tenant upon demand.

9.5 **Insurance of Tenant's Contractors and Agents.** In addition to any other insurance requirements, Tenant expressly agrees that none of its agents, contractors, workmen, mechanics, suppliers or invitees performing construction or repair work in the Premises shall commence such work unless and until each of them shall furnish Landlord with satisfactory evidence of insurance coverage, financial responsibility and appropriate written conditional releases of mechanic's or materialmen's lien claims, in advance of contracted work, as necessary.

9.6 **Waiver of Subrogation.** Tenant and Landlord shall cause the insurance companies issuing their respective property (first party) insurance to waive any subrogation rights that those companies may have against Tenant or Landlord, respectively, as long as the insurance is not invalidated by the waiver. If the waivers of subrogation are contained in their respective insurance policies, Landlord and Tenant waive any right that either may have against the other on account of any loss or damage

to their respective property to the extent that the loss or damage is insured under their respective insurance policies.

9.7 **Landlord's Insurance.** Landlord shall maintain throughout the Term liability and property damage insurance comparable to or exceeding the coverage and amounts of insurance carried by reasonably prudent landlords of comparable buildings and workers' compensation coverage as required by law. If Landlord so chooses, Landlord may maintain "Loss of Rents" insurance, insuring that the Rent will be paid in a timely manner to Landlord for a period of at least twelve (12) months if the Premises or the Building or any portion thereof are destroyed or rendered unusable or inaccessible by any cause insured against under this Lease.

## ARTICLE X

### ASSIGNMENT AND SUBLETTING

10.1 **Landlord's Consent Required.** Tenant shall not directly or indirectly, voluntarily or involuntarily, by operation of law or otherwise, assign, mortgage, pledge, encumber or otherwise transfer this Lease, or permit all or any part of the Premises to be subleased or used or occupied for any purpose by anyone other than Tenant without the prior written consent of Landlord, which consent shall not be unreasonably withheld, delayed or conditioned. Any assignment or sublease without Landlord's prior written consent shall, at Landlord's option, be void and shall constitute an Event of Default entitling Landlord to terminate this Lease and to exercise all other remedies available to Landlord under this Lease and at law. Notwithstanding anything to the contrary contained herein, Tenant shall be permitted to assign this Lease and to sublet the Premises in whole or in part to any Affiliate of Tenant without Landlord consent ("**Permitted Transfer**").

10.2 **Basis for Withholding Consent.** Landlord agrees that it will not unreasonably withhold, delay or condition its consent to Tenant's assigning this Lease or subletting the Premises. In addition to other reasonable bases, Tenant hereby agrees that Landlord shall be deemed to be reasonable in withholding its consent if: (i) there exists an Event of Default (as defined in Section 16.1) at the time of request for consent or on the effective date of such subletting or assigning; (ii) the proposed subtenant or assignee seeks to use any portion of the Premises for a use not consistent with other uses in the Building, or is financially incapable of assuming the obligations of this Lease; (iii) the assignment or subletting would materially increase the operating costs for the Building; (iv) the assignment or subletting may conflict with the terms of any easement, covenant, condition or restriction or other agreement affecting the Real Property; or (v) the assignment or sublease would involve a change in use from that expressly permitted under this Lease.

Tenant shall submit to Landlord the name of a proposed assignee or subtenant, the terms of the proposed assignment or subletting, the nature of the proposed subtenant's or

assignee's business, and such information as to the assignee's or subtenant's financial responsibility and general reputation as Landlord may reasonably require.

**10.3 No Release of Obligations.** The consent by Landlord to an assignment or subletting hereunder shall not relieve Tenant or any assignee or subtenant from the requirement of obtaining Landlord's express prior written consent to any other or further assignment or subletting. No subtenant may assign its sublease, or further sublet its subleased premises, without Landlord's prior written consent, which consent may be withheld in Landlord's sole discretion. Neither an assignment or subletting nor the collection of rent by Landlord from any person other than Tenant shall be deemed a waiver of any of the provisions of this Article or release Tenant from its obligations to comply with this Lease, and Tenant shall remain fully and primarily liable for all of Tenant's obligations under this Lease.

**10.4 Permitted Assignment to Affiliates.** Provided that no Event of Default, or event which with the passage of time or the giving of notice would constitute an Event of Default, exists under this Lease, Tenant may, without Landlord's consent, assign or sublet all or a portion of this Lease or the Premises to an Affiliate of Tenant or to any non-affiliated entity with which Tenant merges or which purchases substantially all of the assets of Tenant, if (i) Tenant notifies Landlord at least fifteen (15) days prior to such assignment or sublease; and (ii) the transferee assumes and agrees in a writing reasonably acceptable to Landlord to perform Tenant's obligations under this Lease and to observe all terms and conditions of this Lease.

**10.5 Administrative Costs of Assignment Transaction.** In connection with any request by Tenant for approval of an assignment or sublease other than a Permitted Transfer, Tenant shall pay Landlord's then standard reasonable processing fee, any taxes or other charges imposed upon Landlord or the Real Property as a result of such assignment or sublease, and shall reimburse Landlord for all reasonable costs, including the reasonable fees of attorneys consulted by Landlord in connection with such assignment or sublease, whether or not such proposed assignment or sublease is consented to by Landlord.

## ARTICLE XI

### DAMAGE AND DESTRUCTION

**11.1 Repair and Restoration; Termination Rights.** If all or part of the Premises is damaged by fire or other casualty, or if the Building is so damaged that access to or use and occupancy of the Premises is materially impaired, within forty-five (45) days of the date of the damage, Landlord shall notify Tenant of the estimated time, in Landlord's reasonable judgment, required for repair or restoration ("**Repair Period**"). If the estimated time is one hundred eighty (180) days or less, Landlord shall proceed promptly and diligently to repair or restore the Premises or the portion of the Building necessary for Tenant's occupancy, and this Lease shall remain in effect, except that for

the time unusable, Tenant shall receive a Rent abatement for that part of the Premises rendered unusable in the conduct of Tenant's business.

If the estimated time for repair or restoration is in excess of one hundred eighty (180) days from the date of the casualty, either Party, at its option exercised by written notice to other Party within sixty (60) days after the date of the casualty, may terminate this Lease as of the date specified by Landlord in the notice, which date shall be not less than twenty-five (25) nor more than forty-five (45) days after the date such notice is given, and this Lease shall terminate on the date specified in the notice. In the event that neither Party elects to terminate this Lease, Landlord shall commence to timely repair the damage, in which case this Lease shall continue in full force and effect.

In either case if Landlord fails to repair the damage by the date that is forty-five (45) days after the end of the Repair Period, then Tenant may give notice to Landlord, within ten (10) business days after the end of the Repair Period terminating this Lease as of the date specified in Tenant's notice, which date shall not be earlier than thirty (30) days after the date of Tenant's termination notice; provided however, if Landlord repairs the damage for which it is responsible within thirty (30) days after receipt of Tenant's termination notice, Landlord may elect to nullify Tenant's termination notice (and thereupon this Lease shall continue in full force and effect) by Landlord's notice of such repair and election given to Tenant on or prior to the expiration of such thirty (30)-day period.

**11.2 Damage Near End of Term.** Notwithstanding anything to the contrary set forth in this Article, if the Premises or the Building are damaged during the last twelve (12) months of the Term, Landlord and Tenant shall each have the option to terminate this Lease by giving written notice to the other of the exercise of that option within thirty (30) days after the damage or destruction, and this Lease shall terminate as of the date specified in such notice, which shall be not before the date of such notice nor more than thirty (30) days after the date of such notice.

**11.3 Rent Apportionment.** If Landlord or Tenant elects to terminate this Lease under this Article XI, Tenant shall pay Rent, prorated on a per diem basis and paid up to the date of the casualty. If the Premises are wholly untenable and this Lease is not terminated, Rent shall abate on a per diem basis from the date of the casualty until the Premises are ready for occupancy by Tenant. If part of the Premises are untenable, Rent shall be prorated on a per diem basis and abated in proportion to the portion of the Premises which is unusable until the damaged part is ready for Tenant's occupancy. Notwithstanding the foregoing, if any damage was caused by the gross negligence or willful misconduct of Tenant, its employees or agents, then, in such event, Tenant agrees that Rent shall not abate or be diminished.

**11.4 Waiver of Statutory Provisions.** The provisions of this Lease, including those in this Article XI, constitute an express agreement between Landlord and Tenant that applies in the event of any damage to the Premises, Building, or Real Property. Tenant therefore, fully waives the provisions of any statute or regulation, including

California Civil Code sections 1932(2) and 1933(4), relating to any rights or obligations concerning any such casualty.

## ARTICLE XII

### CONDEMNATION

12.1 **Total Taking - Termination.** If title to the Premises or so much thereof is taken through the exercise of any government power (by legal proceedings or otherwise) by any public or quasi-public authority or by any other party having the right of eminent domain, or by a voluntary sale or transfer either under threat of exercise of eminent domain or while legal proceedings for eminent domain are pending so that reconstruction of the Premises will not result in the Premises being reasonably suitable for Tenant's continued occupancy for the uses and purposes permitted by this Lease, this Lease shall terminate as of the date possession of the Premises or part thereof is so taken.

12.2 **Partial Taking.** If any part of the Premises is taken through the exercise of eminent domain (or is voluntarily conveyed under the threat thereof) and the remaining part is reasonably suitable for Tenant's continued occupancy for the uses and purposes permitted by this Lease, this Lease shall as to the part so taken terminate as of the date that possession of such part of the Premises is taken and the Rent shall be reduced in the same proportion that the floor area of the portion of the Premises taken (less any addition thereto by reason of any reconstruction) bears to the original floor area of the Premises as reasonably determined by Landlord or Landlord's architect. Landlord shall, at its own cost and expense, make all necessary repairs or alterations to the Premises so as to make the portion of the Premises not taken a complete unit.

12.3 **No Apportionment of Award.** All condemnation awards and similar payments shall be paid and belong to Landlord, except for any amounts awarded or paid specifically to Tenant for leasehold improvements, removal and reinstallation of Tenant's trade fixtures and personal property, Tenant's moving costs and Tenant's goodwill. It is expressly understood and agreed by Tenant that except as otherwise stated in this section, Landlord shall be entitled to the entire award for any partial or total taking.

12.4 **Temporary Taking.** No temporary taking of the Premises (which shall mean a taking of all or any part of the Premises for one hundred eighty (180) days or less) shall terminate this Lease or give Tenant any right to any abatement of Rent. Any award made to Tenant by reason of such temporary taking shall belong entirely to Tenant, and Landlord shall not be entitled to share therein.

## ARTICLE XIII

### SUBORDINATION AND ESTOPPEL

13.1 **Estoppel Certificate.** From time to time and within fifteen (15) days after request by Landlord, Tenant shall execute and deliver a certificate to any proposed lender or purchaser, or to Landlord, certifying, with any appropriate exceptions, (a) that this Lease is in full force and effect without modification except as noted, (b) the amount, if any, of prepaid rent and deposits paid by Tenant to Landlord (and not returned to Tenant), (c) the nature and kind of concessions, rental or otherwise, if any, which Tenant has received or is entitled to receive, (d) that, to Tenant's knowledge, Landlord has performed all of its obligations due to be performed under this Lease and that there are no defenses, counterclaims, deductions or offsets outstanding or other excuses for Tenant's performance under this Lease as of such date, and (e) any other fact reasonably requested by Landlord or such proposed lender or purchaser.

13.2 **Subordination and Attornment.** Tenant agrees that this Lease is subject and subordinate to (i) the lien of any mortgage, deed of trust or other encumbrance of the Building or the Real Property, (ii) all present and future ground or underlying leases of the Building or Real Property now or hereafter in force against the Building or Real Property, and (iii) all renewals, extensions, modifications, consolidations, and replacements of the items described in clauses (i) and (ii), provided that the mortgagee or beneficiary thereunder agrees that so long as no Event of Default exists, (a) Tenant's possession of the Premises and rights and privileges under this Lease shall not be diminished or interfered with by such mortgagee or beneficiary during the term of this Lease or any extensions or renewals hereof, and (b) such mortgagee or beneficiary or lessor will not join Tenant as party for the purpose of terminating or otherwise affecting Tenant's interest in this Lease in any action of foreclosure or other proceeding to enforce any rights arising out of any default under any mortgage or deed of trust.

13.3 **Subordination Agreement.** The subordination described in this Article XIII is self-operative, and no further instrument of subordination shall be required to make it effective. To confirm this subordination, however, Tenant shall, within fifteen (15) days after Landlord's request, execute any further instruments or assurances in recordable form that Landlord reasonably considers necessary to evidence or confirm the subordination of this Lease to any such encumbrances or underlying leases, provided that that any such instrument provides that the mortgagee or the beneficiary agrees that so long as no Event of Default exists, (a) Tenant's possession of the Premises and rights and privileges under this Lease shall not be diminished or interfered with by such mortgagee or beneficiary during the term of this Lease or any extensions or renewals hereof, and (b) such mortgagee or beneficiary will not join Tenant as a party for the purpose of terminating or otherwise affecting Tenant's interest in this Lease in any action of foreclosure or other proceeding to enforce any rights arising out of any default under any mortgage or deed of trust. Tenant shall have no obligation to execute any instrument subordinating its rights hereunder to the lien of any mortgage or deed of trust unless such instrument contains the foregoing conditions. Tenant's failure to execute and deliver such instrument(s) shall constitute a default under this Lease.

13.4 **Attornment.** Tenant covenants and agrees to attorn to the transferee of Landlord's interest in the Real Property or the Building by foreclosure, deed in lieu of

foreclosure, exercise of any remedy provided in any encumbrance or underlying lease affecting the Building or the Real Property, or operation of law (without any deductions or setoffs), if requested to do so by the transferee, and to recognize the transferee as the lessor under this Lease. The transferee shall not be liable for any acts, omissions, or defaults of Landlord that occurred before the sale or conveyance other than acts, omissions or defaults that are continuing upon transferee's acquisition of the Real Property and transferee fails to cure the same after receiving notice thereof.

13.5 **Notice of Default; Right to Cure.** Tenant agrees to give written notice of any default by Landlord to the holder of any encumbrance or underlying lease affecting the Building or the Real Property, provided that Tenant has received written notice of the name and address of such encumbrance holder or lessor. Tenant agrees that, before it exercises any rights or remedies under the Lease, the lienholder or lessor shall have the right, but not the obligation, to cure the default within the same time, if any, given to Landlord to cure the default, plus an additional thirty (30) days. Tenant agrees that this cure period shall be extended by the time (not to exceed an additional sixty (60) days) necessary for the lienholder to begin foreclosure proceedings and to obtain possession of the Building or Real Property, as applicable.

13.6 **Nondisturbance.** Landlord agrees to use commercially reasonable efforts to obtain from the holder of any existing and future indebtedness secured by the Building, a subordination, nondisturbance and attornment agreement which provides that in the event of foreclosure or transfer in lieu of foreclosure, so long as no default by Tenant has occurred under this Lease and remains uncured beyond any applicable cure period (i) Tenant shall not be named or joined in any proceeding that may be instituted to foreclose or enforce the mortgage unless such joinder is legally required to perfect such proceeding, and (ii) Tenant's possession and use of the Premises in accordance with the provisions of the Lease shall not be affected or disturbed by reason of the subordination to or any modification of or default under the mortgage.

## ARTICLE XIV

### SURRENDER OF PREMISES; HOLDING OVER

14.1 **Surrender of Premises.** On expiration of this Lease, Tenant shall surrender the Premises in the same condition as when the Term commenced, ordinary wear and tear excepted. Except for furniture, equipment and trade fixtures (other than those which are affixed to the Premises so that they cannot be removed without material damage to the Premises) all alterations, additions or improvements, whether temporary or permanent in character, made in or upon the Premises, either by Landlord or Tenant, shall be Landlord's property and at the expiration or earlier termination of the Lease shall remain on the Premises without compensation to Tenant; provided that, upon reasonable written request of Landlord, Tenant shall, at its expense and without delay, remove any alterations, additions or improvements (including, without limitation, all telecommunications equipment and cabling, and all alterations and improvements made by Tenant after the Commencement Date) made to the Premises by Tenant and

designated by Landlord to be removed, and shall repair any damage to the Premises or the Building caused by such removal. Notwithstanding the foregoing, Tenant shall have no obligation to remove the initial Tenant Improvements constructed pursuant to Sections 1.15 and 17.2 and Exhibit B hereto upon expiration of the Term of this Lease. If Tenant fails to complete any removal required by this section or to repair the Premises, Landlord may complete such removal and repair, and Tenant shall reimburse Landlord therefor. If Tenant fails to remove such property as required under this Lease, Landlord may dispose of such property in its sole discretion without any liability to Tenant, and further may charge the cost of any such disposition to Tenant.

**14.2 Hold Over Tenancy.** If Tenant remains in possession of the Premises after the expiration or earlier termination of this Lease with Landlord's written consent, Tenant shall be deemed, at Landlord's option, to occupy the Premises as a tenant from month-to-month. During such tenancy (and prior to any termination by Landlord), Tenant agrees to pay Landlord, monthly in advance, an amount equal to: (a) during the first ninety (90) days of such tenancy One Hundred Twenty Five Percent (125%) of all Base Rent which would become due during the last month of the Term, together with all other amounts payable by Tenant to Landlord under this Lease, and (b) for any period following the first ninety (90) days of such tenancy, One Hundred Fifty Percent (150%) of all Base Rent which would become due during the last month of the Term, together with all other amounts payable by Tenant to Landlord under this Lease. Except as provided in the preceding sentence, such month-to-month tenancy shall be on the same terms and conditions of this Lease except that any renewal options, expansion options, rights of first refusal or any other rights or options pertaining to additional space in the Building contained in this Lease shall be deemed to be terminated and shall be inapplicable thereto. Landlord's acceptance of Tent after such holding over with Landlord's written consent shall not result in any other tenancy or in a renewal of the initial term of this Lease.

If Tenant remains in possession of the Premises after the expiration or earlier termination of this Lease without Landlord's written consent, Tenant's continued possession shall be on the basis of a tenancy at sufferance and Tenant shall pay monthly Rent during the holdover period in an amount equal to two hundred percent (200%) of all Base Rent which would become due the last month of the Term, together with all other amounts payable by Tenant to Landlord.

**14.3 No Relocation Benefits.** Tenant acknowledges that pursuant to the California Uniform Relocation Act, Government Code Section 7260, et seq. ("**Relocation Act**"), a commercial tenant that is displaced as a result of a public project may be entitled to certain relocation benefits, including advisory assistance, actual and reasonable moving expenses, and reasonable and necessary reestablishment expenses (collectively, "**Relocation Benefits**"). Tenant hereby knowingly and voluntarily forever waives, discharges and releases any potential claims to Relocation Benefits under the Relocation Act arising out of the termination, expiration, or non-renewal of this Lease, and further voluntarily and knowingly forever waives, releases and discharges Landlord, its related entities and its officers, employees, agents and volunteers from any and all

rights, demands, liabilities, claims, obligations or causes of action in law or equity of whatever kind or nature, whether known or unknown, and whether now existing or hereafter arising, which arise from or relate in any manner to the future expiration, termination, or non-renewal of this Lease, including but not limited to any claims for Relocation Benefits under the Relocation Act and any applicable federal law. This indemnification shall survive the expiration, termination or non-renewal of this Lease.

Tenant is aware of and familiar with the provisions of California Civil Code Section 1542 which provide:

**A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS WHICH THE CREDITOR DOES NOT KNOW OR SUSPECT TO EXIST IN HIS OR HER FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH IF KNOWN BY HIM OR HER MUST HAVE MATERIALLY AFFECTED HIS OR HER SETTLEMENT WITH THE DEBTOR.**

Tenant hereby waives and relinquishes all rights and benefits which it may have under California Civil Code Section 1542.

\_\_\_\_\_  
Tenant's Initials

## ARTICLE XV

### LANDLORD'S RESERVED RIGHTS.

15.1 **Rights Reserved to Landlord.** Without notice and without liability to Tenant, and without effecting an eviction or disturbance of Tenant's use or possession, Landlord shall have the right to (i) grant utility easements or other easements in, or subdivide or make other changes in the legal status of the Land, the Building or the Real Property as Landlord shall deem appropriate in its sole discretion, provided such changes do not substantially interfere with Tenant's use of the Premises for the Permitted Use; (ii) enter the Premises at reasonable times and with reasonable advance notice (and at any time in the event of an emergency), to inspect (including inspections by prospective lenders for or buyers of the Real Property), or repair the Premises or the Building and to perform any acts related to the safety, protection, reletting, sale or improvement of the Premises or the Building; (iii) install and maintain "For Sale" signs on and in the Building and the Real Property and "For Lease" signs during the last one hundred eighty (180) days of the initial lease term, or alternatively the last one hundred eighty (180) days of the exercised option period; and (iv) make such rules and regulations as, in the reasonable judgment of Landlord, may be needed from time to time for the safety of the tenants, the care and cleanliness of the Premises, the Building and the Real Property and the preservation of good order therein. Landlord shall at all times retain a key with which to unlock all of the doors in the Premises, except Tenant's vaults and safes. If an

emergency necessitates immediate access to the Premises, Landlord may use whatever force is necessary to enter the Premises and any such entry to the Premises shall not constitute a forcible or unlawful entry into the Premises, a detainer of the Premises or an eviction of Tenant from the Premises or any portion thereof.

## ARTICLE XVI

### DEFAULT AND REMEDIES

16.1 **Tenant's Default.** It shall be an "Event of Default" hereunder if Tenant shall:

(a) fail to pay when due any monthly installment of Rent (or, if applicable under this Lease, Operating Expenses), or fail to pay any other amount owed by Tenant to Landlord under this Lease as and when due and such failure continues for five (5) days following written notice thereof to Tenant by Landlord;

(b) fail to provide any certificate, instrument or assurance as required pursuant to Article IX if the failure continues for five (5) days after written notice of the failure from Landlord to Tenant;

(c) make a general assignment for the benefit of its creditors or file a petition for bankruptcy or other reorganization, liquidation, dissolution or similar relief;

(d) have a proceeding filed against Tenant seeking any relief mentioned in (c) above which is not discharged within sixty (60) days thereafter;

(e) have a trustee, receiver or liquidator appointed for Tenant or a substantial part of its property;

(f) abandon the Premises for more than three (3) consecutive months;

(g) assign this Lease or sublease any portion of the Premises in violation of Article X; or

(h) fail to comply with any other provision of this Lease in the manner required hereunder and such failure continues for thirty (30) days after written notice thereof to Tenant by Landlord (or if the noncompliance cannot by its nature be cured within the thirty (30)-day period, if Tenant fails to commence to cure such noncompliance within the thirty (30)-day period and thereafter diligently prosecute such cure to completion).

16.2 **Remedies on Default.** Upon the occurrence of an Event of Default, Landlord shall have the right to pursue any one or more of the following remedies in

addition to any other remedies now or later available to Landlord at law or in equity. These remedies are not exclusive but instead are cumulative.

(a) **Continue Lease.** Landlord may continue this Lease in full force and effect. In such case, so long as Landlord does not terminate Tenant's right to possession, the Lease will continue in effect and Landlord shall have the right to collect Rent when due, and may undertake efforts to relet the Premises, or any part of them, to third parties for Tenant's account. Tenant shall be liable to Landlord for all reasonable costs Landlord incurs in reletting the Premises including, without limitation, broker's commissions, expenses of remodeling the Premises required by the reletting, and like costs. Reletting can be for a period shorter or longer than the remaining term of this Lease. Tenant shall pay to Landlord the Rent due under this Lease on the date the Rent is due, less the Rent Landlord receives from any reletting. No act by Landlord allowed by this section shall terminate this Lease unless Landlord terminates Tenant's right to possession. After an Event of Default and for as long as Landlord does not terminate Tenant's right to possession of the Premises, if Tenant obtains Landlord's consent, Tenant shall have the right to assign or sublet its interest in this Lease, but Tenant shall not be released from liability.

(b) **Terminate Lease.** Landlord may terminate the Lease and Tenant's right to possession of the Premises at any time following an Event of Default. No act by Landlord other than giving written notice to Tenant shall terminate this Lease. Acts of maintenance, efforts to relet the Premises or the appointment of a receiver on Landlord's initiative to protect Landlord's interest under this Lease shall not constitute a termination of Tenant's right to possession. On termination, Landlord shall have the right to recover from Tenant all of the following:

(i) The worth, at the time of the award, of any unpaid Rent that had been earned at the time of termination of this Lease;

(ii) The worth, at the time of the award, of the amount by which the unpaid Rent that would have been earned after the date of termination of this Lease until the time of the award exceeds the amount of the unpaid Rent that Tenant proves could have been reasonably avoided;

(iii) The worth, at the time of the award, of the amount by which the unpaid Rent for the balance of the Term after the time of the award exceeds the amount of unpaid Rent that Tenant proves could have been reasonably avoided;

(iv) Any other amount necessary to compensate Landlord for all detriment proximately caused by Tenant's failure to perform obligations under this Lease, including, without limitation, brokerage commissions, advertising expenses, expenses of remodeling the Premises for a new tenant, and any special concessions made to obtain a new tenant; and

(v) Any other amounts, in addition to or in lieu of those listed above that may be permitted by law.

“The worth, at the time of the award” as used in clauses (i) and (ii) of this Paragraph (b), is to be computed by allowing interest at the maximum rate allowed by law at that time, or if there is no such maximum, at a rate of ten percent (10%) per annum. “The worth, at the time of the award,” as referred to in clause (iii) of this Paragraph (b) is to be computed by discounting the amount at the discount rate of the Federal Reserve Bank of San Francisco at the time of the award plus one percent (1%).

(c) **Receiver.** Landlord shall have the right to have a receiver appointed to collect Rent. Neither the filing of a petition for the appointment of a receiver nor the appointment itself shall constitute an election by Landlord to terminate this Lease.

16.3 **Landlord’s Default.** Landlord’s failure to perform any of its obligations under this Lease shall constitute a Landlord Event of Default hereunder if the failure continues for thirty (30) days after written notice of the failure from Tenant to Landlord. If the required performance cannot be completed within thirty (30) days, Landlord’s failure to perform shall not constitute a Landlord Event of Default if Landlord undertakes to cure the failure within such thirty (30)-day period and diligently and continuously attempts to complete the cure as soon as reasonably possible. Tenant waives any right to terminate this Lease and to vacate the Premises upon Landlord’s default under this Lease. Tenant’s sole remedy on Landlord’s default is an action for damages or injunctive or declaratory relief.

## ARTICLE XVII

### TENANT IMPROVEMENTS; PARKING

17.1 **Parking.** Landlord hereby grants to Tenant an exclusive license and right to use the parking area located on the Real Property for vehicular parking, such exclusive license to be appurtenant to Tenant’s leasehold estate created by this Lease. Tenant may use up to one hundred forty-one (141) parking spaces in Landlord’s surface parking lot. There shall be no overnight parking of any vehicles, and vehicles which have been parked in violation of the terms hereof may be towed away at the owner’s expense. Tenant shall not permit or allow any vehicles that belong to or are controlled by Tenant or Tenant’s employees, suppliers, shippers, customers or invitees to be loaded, unloaded, or parked in areas other than those designated by Landlord for such activities.

17.2 **Tenant Improvements; Tenant Improvement Allowance.** Landlord shall provide a Tenant Improvement Allowance in the amount of Five Hundred Thousand Dollars (\$500,000) as a Rent credit over the three-year Term. The Rent credit shall be

deducted from the scheduled monthly Base Rent at a rate of Thirteen Thousand Eight Hundred Eighty Nine Dollars (\$13,889) per month. This allowance shall be used to construct the Tenant Improvements as described in Exhibit B. The obligations of Landlord and Tenant, with respect to the Tenant Improvements, including without limitation Tenant's obligation to pay for such work and provide third-party invoices and written evidence of Tenant's payment therefor, are set forth in the Work Letter attached hereto as Exhibit B.

## ARTICLE XVIII

### MISCELLANEOUS

18.1 **No Waiver.** No receipt and retention by Landlord of any payment tendered by Tenant in connection with this Lease shall constitute an accord and satisfaction, or a compromise or other settlement, notwithstanding any accompanying statement, instruction or other assertion to the contrary unless Landlord expressly agrees to an accord and satisfaction, or a compromise or other settlement, in a separate writing duly executed by Landlord. Landlord will be entitled to treat any such payments as being received on account of any item or items of Rent, interest, expense or damage due in connection herewith, in such amounts and in such order as Landlord may determine at its sole option. Failure of either Party to exercise any right in one or more instance shall not be construed as a waiver of the right to strict performance or as an amendment to or modification of this Lease. Any waiver of any condition or provision set forth in this Lease shall not be deemed a waiver of any subsequent breach of such condition or provision or of any other condition or provision, nor shall any such waiver be deemed a continuing waiver.

18.2 **Severability.** The Parties intend this Lease to be legally valid and enforceable in accordance with all of its terms to the fullest extent permitted by law. If an arbitrator or a court of competent jurisdiction holds any provision hereof to be invalid or unenforceable in whole or in part for any reason, the validity and enforceability of the remaining clauses, or portions of them, shall not be affected unless an essential purpose of this Lease would be defeated by loss of the invalid or unenforceable provision.

18.3 **Governing Law; Construction.** This Lease shall be construed according to the laws of the State of California without regard to principles of conflict of laws. The parties acknowledge that this Lease is the product of negotiation and compromise on the part of both parties, and agree that the provisions hereof shall be construed in accordance with their fair meaning and not in accordance with any rule providing for interpretation against the party who causes the uncertainty to exist or against the drafter. The captions used for the Sections and Articles of this Lease have been inserted for convenience only and shall not be used to alter or interpret the content of this Lease.

18.4 **Binding Effect; Survival.** The covenants, conditions, warranties and agreements contained in this Lease shall be binding upon and inure to the benefit of the parties and their respective successors and permitted assigns. The representations and

warranties of Landlord and Tenant and the indemnification obligations of Landlord and Tenant set forth herein shall survive the expiration or termination of this Lease as shall all other provisions hereof which are intended to survive such expiration or termination.

18.5 **Time.** Time is of the essence of each provision of this Lease.

18.6 **Entire Agreement; Amendments.** This Lease and Exhibits A and B attached hereto and incorporated herein by this reference, constitutes the final, complete, and exclusive statement of the terms of the agreement between Landlord and Tenant pertaining to the lease of Real Property, the Premises and space in the Building and supersedes all prior and contemporaneous understandings or agreements of the parties. This Lease may not be amended or modified except in a writing signed by both parties.

18.7 **Notices.** All notices delivered pursuant to this Lease shall be in writing and delivered to Landlord or Tenant at the applicable addresses designated in Sections 1.1 and 1.3 or to such other address as may hereafter be designated by either Party by written notice delivered to the other Party in accordance with this Section. Such notices shall be effective upon receipt or refusal of delivery. Such notices shall be sent by (i) United States mail, certified mail with return receipt requested, or (ii) overnight delivery service.

18.8 **Force Majeure.** Except as otherwise provided in this Lease, the time for performance of an obligation other than the payment of money under this Lease shall be extended for the period during which a Party is prevented from performing due to Unavoidable Delay. “Unavoidable delay” shall mean any and all delay beyond the applicable Party’s reasonable control, including without limitation, delays caused by the other Party; governmental restrictions, regulations, controls, preemptions or delays; orders of civil, military or naval authorities; strikes, labor disputes, lock-outs, shortages of labor or materials or reasonable substitutes therefore; Acts of God; fire, earthquake, floods, explosions or other casualties; extreme weather conditions or other actions of the elements; enemy action, civil commotion, riot or insurrection.

18.9 **Attorneys’ Fees; Prejudgment Interest.** If the services of an attorney are required by either Party to secure the performance hereof or otherwise upon the breach or default of the other Party, or if any judicial remedy is necessary to enforce or interpret any provision of this Lease, or if the services of an attorney are required upon the bankruptcy of a Party to this Lease to compel or object to assumption or rejection of this Lease, seek relief from the automatic stay or object to an action to recover a preference or fraudulent transfer, the prevailing Party shall be entitled to reasonable attorneys’ fees, costs, expert witnesses fees, post judgment collection costs, and other expenses, in addition to any other relief to which such Party may be entitled. Any award of damages following judicial remedy as a result of the breach of this Lease or any of its provisions shall include an award of prejudgment interest from the date of the breach at the maximum amount of interest allowed by law.

18.10 **Authority.** Each Party warrants and represents that it has full authority to enter into this Lease, that this Lease constitutes a binding obligation of such Party, and that the individual(s) signing on behalf of such Party are duly authorized to bind such Party hereto. In that regard, Landlord represents that title to the Real Property was previously conveyed from the Redevelopment Agency of the City of South San Francisco, a public body, corporate and politic, to the City of San Francisco, a municipal corporation, prior to the dissolution of the Redevelopment Agency effective February 1, 2012. By operation of law, real property held by the former Redevelopment Agency is or will be transferred to the Agency as successor in interest. The governing bodies of the Agency and the City agree to take such actions as may be necessary to approve, affirm or ratify this Lease.

18.11 **Landlord Approvals.** Whenever the consent or approval of Landlord is required hereunder, such consent or approval may be granted or withheld by the Agency Executive Director/City Manager or his or her designee, unless the Agency Executive Director/City Manager determines in his or her discretion that such matter shall be referred to the Agency/City governing board(s) for consideration.

18.12 **Counterparts.** This Lease may be executed in counterparts, each of which shall constitute an original, and all of which together shall constitute one and the same instrument. The signature page of any counterpart may be detached therefrom without impairing the legal effect of the signature(s) thereon provided such signature page is attached to any other counterpart identical thereto except having additional signature pages executed by any other Party. This Lease shall take effect when signed by all Parties hereto and all Parties have written notice of the signature of all the remaining Parties. The Parties agree that a signed copy of this Lease transmitted by one Party to the other Party by facsimile transmission shall be binding upon the sending Party to the same extent as if it had delivered a signed original of the Lease.

18.13 **Brokers.** Tenant and Landlord each represent and warrant to the other that except as stated in this Section, no broker or agent is entitled to a broker's commission or finder's fee in connection with the execution of this Lease or the consummation of the transaction contemplated hereby, and each Party agrees to defend and indemnify the other Party against any loss, expense or liability incurred by the other Party as a result of a breach of such representation and warrant. The provisions of this Section shall survive the expiration or earlier termination of the Lease and the Landlord shall have no liability therefor. Without limiting the foregoing, Tenant's obligation to defend and indemnify shall include defense and indemnification of Landlord with respect to any claims, charges, finder's fees, commissions, costs or other liabilities claimed by Victor M. Catanzaro and/or Wall Street Properties in connection with the execution of this Lease or the consummation of the transaction contemplated hereby. The terms of this Section shall survive the expiration of the earlier termination of this Lease.

18.14 **Submission of Lease.** Submission of this document for examination or signature by the Parties does not constitute an option or offer to lease the Premises on the terms in this document or a reservation of the Premises in favor of tenant. This document

is not effective as a lease or otherwise until executed and delivered by both Landlord and Tenant.

18.15 **Non-Agency.** It is not the intention of Landlord or Tenant to create hereby a relationship of principal and agent, and under no circumstances shall Tenant be considered the agent of Landlord, it being the sole purpose and intent of the Parties to create a relationship of landlord and tenant.

18.16 **No Merger.** The voluntary or other surrender of this Lease by Tenant or a mutual cancellation thereof, or a termination by Landlord, shall not work a merger, and shall at the option of Landlord terminate all or any existing subtenancies or may at the option of Landlord, operate as an assignment to Landlord of any or all such subtenancies.

NOW THEREFORE, Landlord and Tenant have executed this Lease as of the date first written above.

**TENANT**

RED CART MARKET INC dba PET CLUB STORES, a California corporation

By: \_\_\_\_\_

Print Name: Tom Lee

Title: Secretary

**LANDLORD**

SUCCESSOR AGENCY TO THE REDEVELOPMENT AGENCY OF THE CITY OF SOUTH SAN FRANCISCO, a public entity

By: \_\_\_\_\_  
Barry M. Nagel

Its: Executive Director

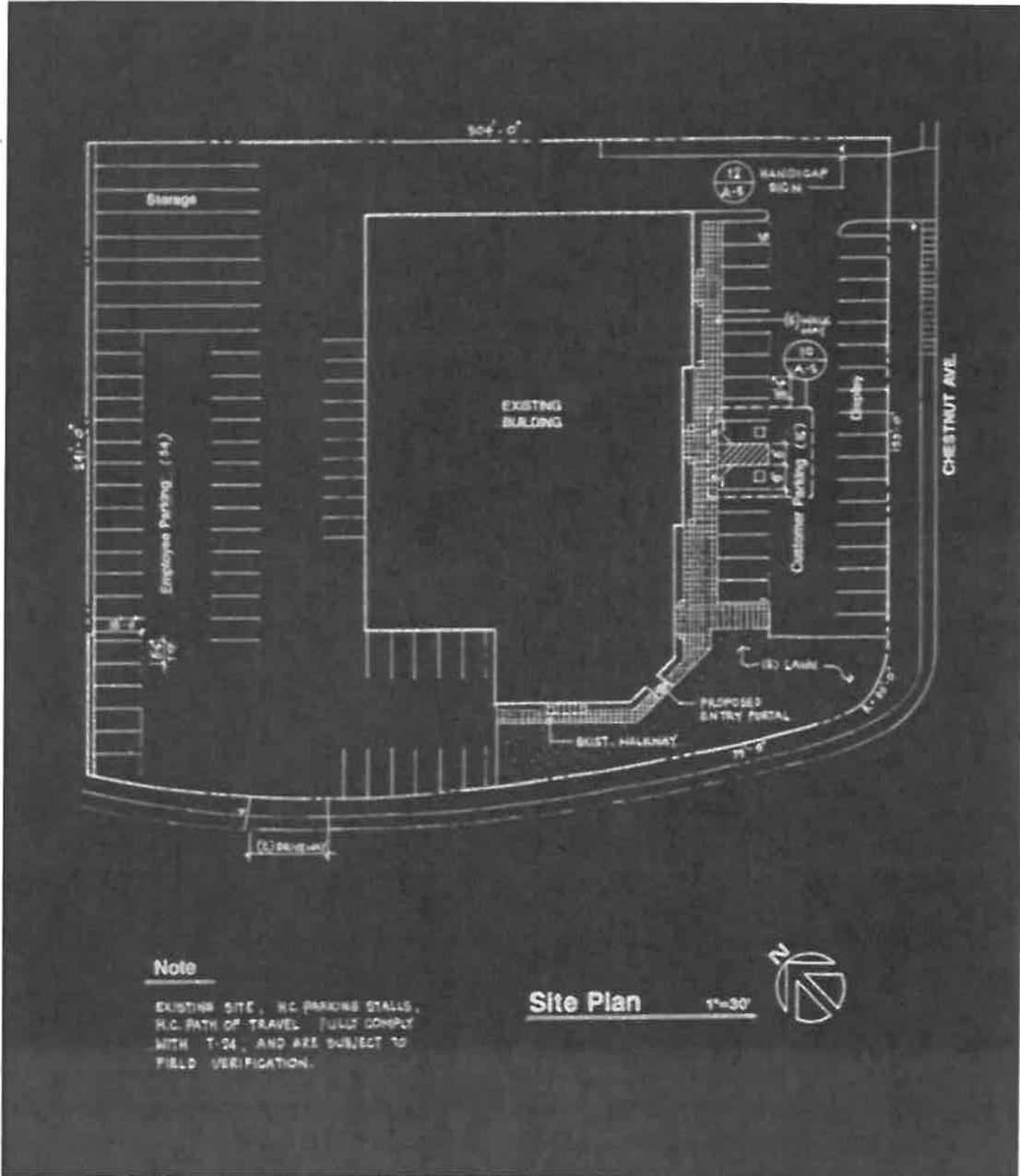
Attest: \_\_\_\_\_  
Krista J. Martinelli, Secretary

Approved as to Form:

\_\_\_\_\_  
Steven T. Mattas, General Counsel

# EXHIBIT A

## DIAGRAM OF PREMISES



## EXHIBIT B

### WORK LETTER

This Work Letter (“**Work Letter**”) shall be deemed a part of, and is hereby incorporated into that certain Lease (the “**Lease**”), dated as of \_\_\_\_\_ by and between the Successor Agency to the Redevelopment Agency of the City of South San Francisco, a public entity, (“**Landlord**”), and Red Cart Market Inc. dba Pet Club Stores, a California corporation (“**Tenant**”). Capitalized terms used but not defined herein shall have the meanings assigned thereto in the Lease.

1. **Plans.**

(a) **Space Plan.** John C. Lee, Tenant’s designated space planner and architect and/or Space Planner’s sub-contractors, engineers or consultants, collectively (“**Space Planner**”), has prepared and delivered to Landlord a space plan for the Real Property and the Premises showing the location of all partitions and doors and the lay-out of the Premises, and a plan for all Tenant Improvements described in Section 17.2 of the Lease).

Landlord shall timely review and approve the space plan for the Premises.

(b) **Compliance With Laws.** Tenant shall cause the construction of the Tenant Improvements to be completed in accordance with all Applicable Laws.

(c) **Construction Plans.** The Tenant shall comply with the Planning Division criteria for a “Complete Application,” identified on the Planning Application. Incomplete applications will not be accepted. If the Planning Division requires additional information, the application process will be delayed. The completed application shall be processed according to the established hearing schedule, which has been determined for the entire calendar year of 2013. Within thirty (30) days after approval of the City’s planning entitlement, Tenant shall deliver a completed building permit application, included completed plan sets and payment of the fees, to the City Building Division. Tenant shall comply with the application criteria listed on the Department of Economic and Community Development, Building Division Plan Submittal Requirements, Residential and Commercial Projects. The foregoing process shall continue until the Construction Plans are approved by the City and the Landlord.

Construction Plans shall be in accordance with Section 1.7, above which states; “90 days after execution by both Parties following City/Successor Agency approval and Successor Agency Oversight Board (“Oversight Board”) adoption of a resolution, plus (a) expiration of the statutory review period for the California Department of Finance (“DOF”) pursuant to Health and Safety Code Section 34181 (h); or (b) expiration of the statutory review period pursuant to Health and Safety Code Section 34181 (f), if so extended by DOF; or (c) the date upon which DOF issues written approval of the

Oversight Board action. Issuance of City entitlements and building permits shall also be a condition of Commencement. Tenant shall cause a complete City permit application together with required site plan, floor plan, elevation drawings, grading and drainage plans, landscaping plan, signage and lighting plans, and other pertinent exhibits and payment of the fees be submitted to the City Planning Division within ten (10) business days from Oversight Board approval of the Lease.”

(d) **Change Orders.** Tenant may request changes in the final Construction Plans and drawings consisting of non-structural additions, deletions, value engineering items or other revisions to the Tenant Improvements and extensions of the progress schedule, which such changes shall be subject to Landlord’s prior written approval, which approval Landlord shall not unreasonably withhold or delayed for non-structural interior changes reasonably requested by Tenant. Within five business (5) days following Tenant’s change request, Landlord shall approve or disapprove such change request, and if approved, the Parties will evidence agreement to such changes by signing change orders (each a “**Change Order**”). Following Landlord’s written approval of a Change Order, Tenant shall diligently prosecute the changes in accordance with the requirements of that Change Order.

### 3. **Construction and Costs of Tenant Improvements:**

(a) **Construction Obligation and Construction Allowance.** Promptly following Landlord’s approval of the Construction Plans, Tenant shall construct the Tenant Improvements in a good and workmanlike manner in accordance with the Construction Plans and all Applicable Laws, using Tenant’s designated personnel and a contractor or contractors reasonably approved in writing by Landlord before the commencement of construction (such contractor or contractors are collectively referred to herein as “**Tenant’s Contractor**”, whether one or more). The cost of the construction of the Tenant Improvements, including the cost of preparing the Space Plan and the Construction Plans, shall be at Tenant’s expense; provided, however, subject to the limitations set forth in this Section, Landlord shall reimburse Tenant for costs actually incurred by Tenant in constructing the foregoing upon submission of invoices and lien waivers reasonably requested by Landlord. Landlord’s obligation to reimburse Tenant for Tenant Improvements shall not exceed a total of Thirteen Thousand Eight Hundred Eighty Nine Dollars (\$13,889) per month during the Lease Term of thirty-six (36) months (the “**Construction Allowance**”). In the event the cost of the Tenant Improvements exceeds the Construction Allowance, such overage shall be borne exclusively by Tenant. Landlord makes no representation or warranty whatsoever as to the total cost of the Tenant Improvements, and Tenant acknowledges that the cost of the Tenant Improvements may exceed the Construction Allowance. The cost of the Tenant Improvements shall include all architectural, space planning and engineering fees, costs of compliance with Applicable Law and any and all licensing or permit fees and the cost of Tenant’s designated personnel to secure and prepare the Real Property for Tenant’s Use and Occupancy. The Construction Allowance shall be used solely for: (i) the sum paid to Tenant’s Contractor for construction of the Tenant Improvements (the “**Contract Sum**”); (ii) the payment of architectural, design, consultant, space planning, and/or engineering

fees; (iii) the payment of any and all costs of Tenant's designated employees and/or independent contractors to secure and prepare the Real Property for Tenant's use and occupancy; (iv) the payment of any and all costs associated with Tenant's acquisition of any and all necessary or convenient fixtures in or about the Real Property (whether temporary or permanent); and/or (v) the payment of any and all licensing or permit fees related to the Tenant Improvements (collectively, the "**Permitted Costs**").

(b) **Payment.** Subject to the following requirements, Landlord shall make progress payments to Tenant as Tenant's Contractor completes the Tenant Improvements in accordance with the Construction Plans. Requests for such disbursements shall be made on the AIA application for payment and such disbursements shall be made no more often than once per thirty (30) days.

(Landlord shall make disbursements to Tenant up to the amount of the Construction Allowance provided all of the following conditions shall have been met according to Landlord's reasonable satisfaction: (1) Landlord shall have received executed lien releases for all work completed as of the date of payment; (2) Landlord shall have received copies of third-party invoices for Tenant Improvements completed and written evidence reasonably satisfactory to Landlord of Tenant's payment of same; and (3) all work completed as of the date of payment shall have been, in Landlord's judgment, completed in a good and workmanlike manner following inspection by Landlord of such work. Tenant shall notify Landlord fifteen (15) days prior to the anticipated date of substantial completion of the Tenant Improvements, at which time Landlord and Tenant shall arrange for Landlord's inspection thereof. Following such inspection Landlord shall have the option to cause an additional punch list to be prepared ("**Landlord's Punch List**") setting forth those items that are not completed and/or that Landlord desires to be corrected. Tenant shall cause Tenant's Contractor to complete and/or remedy the items set forth in Landlord's Punch list within thirty (30) days after the delivery of Landlord's Punch List.

(c) **Excess Costs.** If the total Permitted Costs for the Tenant Improvements or exceeds the Construction Allowance, then Tenant, at its sole cost and expense, shall pay all such excess costs ("**Excess Costs**") to the appropriate party and contractor(s). Landlord makes no representation or warranty whatsoever as to the total costs of the Tenant Improvements and Tenant acknowledges that the costs thereof may exceed the Construction Allowance.

(d) **Liens Arising from Excess Costs.** Tenant agrees to keep the Premises and the Building free from liens arising out of any construction performed by Tenant pursuant to this Work Letter or the Lease. In the event that any such lien is filed, Tenant shall immediately cause the same to be released of record, and if within fifteen (15) days following such filing Tenant fails to cause the same to be released of record by payment or posting of a proper bond, Landlord shall have, in addition to all other remedies provided herein, in the Lease, or under law, the right, but not the obligation, to cause the same to be released by such means as it in its sole discretion deems proper, including payment of or defense against the claim giving rise to such lien. All sums paid by

Landlord in connection therewith shall constitute Rent under the Lease and a demand obligation of Tenant to Landlord, and such obligation shall bear interest at the rate of ten percent (10%) per annum from the date of payment by Landlord until the date paid by Tenant.

5. **Insurance.** On or before the commencement of construction of the Tenant Improvements, Tenant, at Tenant's sole cost and expense, shall obtain and thereafter maintain, all insurance required by Section 9.2 of the Lease, in the form required pursuant to the Lease. In addition to such insurance, Tenant's Contractor, at its sole cost and expense (and not as a Permitted Cost unless part of the Contract Sum), shall obtain and maintain commercial general liability insurance coverage, builder's risk insurance, and workmen's compensation insurance, all in amounts and with companies and on forms as Landlord may consider reasonable or appropriate for its protection. Such liability insurance shall name the Indemnitees as additional insureds, and the builder's risk insurance shall name Tenant, Landlord and Landlord's mortgagee (if any) as loss payee. Tenant shall deliver to Landlord evidence of such insurance, including duplicate copies of such insurance policies if requested by Landlord, prior to the commencement of construction of the Tenant Improvements.

6. **Indemnity.** Tenant does hereby assume all risk of loss or damage to its machinery, equipment, fixtures, and other personal property and agrees to indemnify, defend (with counsel reasonably acceptable to Landlord), and hold the Indemnitees harmless from all Claims relating to loss or damage to such property, and all Claims relating to or arising from any injury to the property of Landlord, and any death or personal injury to any person or persons arising out of Tenant's and/or Tenant's Contractor's construction work in or about the Premises or the Building (except to the extent arising from the gross negligence or willful misconduct of Landlord or its agents).

7. **Construction Representatives.** Landlord's and Tenant's representatives for coordination of construction and approval of plans, improvement inspections, progress payments (Construction Allowance), and change orders will be as follows, provided that either Party may change their respective representative upon three (3) days' written notice to the other:

Landlord's Representative: Michael Lappen  
400 Grand Avenue  
South San Francisco, Ca 94080

mike.lappen@ssf.net tel. 650-829-6690

Tenant's Representative: John C. Lee Architects  
711 San Miguel Lane  
Foster City, Ca 94404

archjcl@gmail.com tel. 650-345-6663

8. **“As Built” Plans.** Within thirty (30) days after completion of the Tenant Improvements, Tenant shall deliver to Landlord two (2) copies of “as built” drawings and plans therefor, together with a CAD disk containing electronic versions of such drawings and plans.

9. **Consent as to General Contractor.** Landlord hereby consents to \_\_\_\_\_ as the general contractor for the construction of the Tenant Improvements.

NOW THEREFORE, Landlord and Tenant have executed this Work Letter as of the date first written above.

**TENANT**

RED CART MARKETING INC, dba PET CLUB STORES, a California corporation

By: \_\_\_\_\_

Print Name: Tom Lee

Title: Secretary

**LANDLORD**

SUCCESSOR AGENCY TO THE REDEVELOPMENT AGENCY OF THE CITY OF SOUTH SAN FRANCISCO, a public entity

By: \_\_\_\_\_

Barry M. Nagel

Its: Executive Director

Attest: \_\_\_\_\_

Krista J. Martinelli, Secretary

Approved as to Form:

\_\_\_\_\_  
Steven T. Mattas, General Counsel

2011044.1

**WALL STREET  
PROPERTIES**  
Commercial Real Estate

October 3, 2012

City of South San Francisco, et al  
c/o Michael Lappen  
Economic Development Department  
400 Grand Avenue  
South San Francisco, Ca 94080

via email delivery  
mike.lappen@ssf.net

re: Amended lease proposal - Pet Club  
1 Chestnut Avenue, South San Francisco, Ca

Dear Michael,

In reply to the lease proposal submitted by Pet Club on August 17, 2012 the City provided a response on September 26, 2012. Pet Club reviewed the City Proposal and unless addressed below the deal points of the 9/26/12 City letter are acceptable to Pet Club and are incorporated herein.

In review, Pet Club commenced business in South San Francisco in 1997 and in the most recent year ending (2011) generated sales tax in excess of \$544,000 to the State. The City directly realized approximately \$65,400 or \$5,450 per month from the sales tax revenue which should be considered as additional rent payable by Pet Club. The base rent offered is \$35,890.00 monthly (before TI / Set Up Allowance), a blended base rental rate of \$1.35/sf/mo (\$16.25 annually) NNN, but as previously mentioned rent for the upper mezzanine space should be either disregarded altogether or reduced significantly, or both. Assuming little or no value to the mezzanine space the effective rent for the ground level space is approximately \$1.67/sf/mo (\$20.00) the higher rent range of retail space.

It should be noted that with the sales tax revenue (\$5,450/mo), the effective base rent is approximately \$41,430.00 monthly to the City and/or beneficiary agencies. A lease with Pet Club will generate approximately \$808,012.00 ( $544,000 + [35,890 - 13,889] \times 12 = 264,012$ ) = 808,012) annually (\$67,334 monthly) payable to the State, City and beneficiary agencies or \$2,424,036 over the three (3) year term.

In consideration of the foregoing and other matters discussed to date we submit the following for consideration and reflected in the Lease Agreement;

**BASE RENT:** The base rental rate shall be **\$35,890.00** per month payable for the lease period beginning at rent commencement (*subject to Tenant Improvement / Set-up Allowance, below*) and continuing each month for thirty-six (36) months.

**TENANT IMPROVEMENT / SET UP AND FIXTURIZE ALLOWANCE:** The Tenant Improvement / Set Up and Fixturize Allowance (TI Allowance) shall be \$500,000 in the form of rent credit. The rent credit shall be deducted from the scheduled monthly rent at a rate of \$13,889.00 per month. ( $500,000 / 36 = 13,889/\text{mo}$ ).

**COMMENCEMENT:** **Occupancy Commencement:** The earlier of; (a) Ninety (90) days from full execution of the Lease Agreement following City Council Approval, or (b) forty-six (46) days from OSB resolution, whichever is the earlier to occur, but not later than December 31, 2012.

City of South San Francisco, et al  
c/o Michael Lappen  
re: Amended lease proposal - Pet Club  
1 Chestnut Avenue.

October 3, 2012  
page 2 of 4

**Rent Commencement:** Rent shall commence Ninety (90) days from issuance of city building permits. Tenant shall make application for building permits; (i) within forty-five (45) days of approval of the OSB by resolution, or (ii) within thirty (30) days after City Council execution of the lease, whichever is the later to occur.

**ENTITLEMENT & PERMITS / EARLY POSSESSION:** Provided Tenant has deposited with Landlord the security deposit and the first month rent together with evidence of Insurance, and provided such early occupancy does not interfere with Landlord's work or current tenant's (PG&E occupancy), Tenant shall be granted occupancy concurrent with lease execution for purposes of installing Tenant's designated trade fixtures and other necessary improvements and time for tenant to prepare improvement plans and obtain necessary permits. Notwithstanding the foregoing early possession will not occur before the OSB & DOF approves the lease which is anticipated to be no more than 45 days following OSB approval by resolution.

**SECURITY DEPOSIT:** Upon execution of the lease Tenant shall pay to Landlord a security deposit in the amount of **THIRTY FIVE THOUSAND EIGHT HUNDRED NINETY (\$35,890.00) Dollars.**

**RENEWAL OPTION:** Landlord shall inform Tenant in writing when the Property is offered for sale and when the Property is sold.

**LANDLORD'S WARRANTEE:** Landlord represents to Tenant that no known hazardous substances or conditions presently exist on, in or under the premises and further warrants the Premises is not the generator or producer of any known hazardous substances nor contributed to or contaminated any adjoining property and further warrants that in the event any such hazardous substance or condition is discovered by Tenant after the date of occupancy that Landlord will correct such condition in a timely manner at the sole cost and expense of Landlord.

**CONDITION OF PROPERTY:** In addition, the premises shall be delivered to Tenant with electrical in good working order and the roof in a water tight condition.

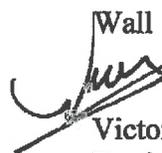
**SIGNS:** Tenant shall have the right to install a sixty (60) foot channel letter "Pet Club" sign at the location designated by Tenant.

Please contact me to discuss any issue raised in this proposal or other issues you feel might need to be addressed. Your consideration and acceptance of this amended offer to lease the Property is appreciated. I look forward to working with you to conclude this element of our transaction.

You can reach me at telephone 650-401-8500 or 650-520-5559.

Very truly yours,

Wall Street Properties



Victor M. Catanzaro  
President

DRE 00531029

**WALL STREET  
PROPERTIES**  
Commercial Real Estate

October 9, 2012

City of South San Francisco  
c/o Michael Lappen  
Economic Development Department  
400 Grand Avenue  
South San Francisco, Ca 94080

*via email delivery*  
mike.lappen@ssf.net

re: lease – amended proposal - Pet Club - *comparables*  
1 Chestnut Avenue, South San Francisco, Ca

Dear Michael,

Last week I presented many rent comparables and other supporting documentation to you and Armando in comparison to 1 Chestnut. The information was obtained from Kidder Mathews Real Estate, CBRE Real Estate, Metrovation Brokerage and The Berube Company, all independent sources, to supplement my email correspondence with Don Krieger of Terranomics of September 27, 2012. Both Don Krieger and Christine Firstenberg (Metrovation) conclude it very unlikely a major tenant would lease retail space of 20,000sf or more for less than 10 years and tenants leasing over 20,000sf normally require options to extend the initial 10 year period. Both Don and Christine state it is quite common for the Landlord to deliver the property in a clean shell (vanilla shell) and provide a tenant improvement allowance.

The tenant improvement allowance provided by landlord (landlord pay in advance of occupancy or credit tenant) cited in the Kidder/Mathews 14 property comparables is between \$28.28 to \$30.00 per square foot leased, or full "Turnkey" improvements. Turnkey being space improved by and at the expense of the landlord to tenant specifications before delivery of the property to tenant.

The majority lease period of the 14 comparables is 10 years, a couple with 20 or 25 year periods. The comparables do not reflect options, but it is most typical for retail leases of this size (20,000sf or more) to include not less than two (2) five (5) year options to extend the lease. Of the 14 K/M comparables 9 are listed at \$1.58/sf/m, or less, only two of the nine are at \$1.58, the other seven (7) are at \$1.50/sf/m or less and the majority include @ \$30.00/sf tenant improvement allowance or full turnkey tenant specified improvements.

Similar to the K/M comparables, the minimum initial lease term stated in the CBRE comparables is ten (10) years. This minimal lease period is affirmed by Don Krieger and Christine Firstenberg. The Berube Company offers 470 Noor Ave, SSF, a 22,000sf space at the asking rate of \$2.00/sf/m, term of 5 years, plus options but it is unlikely major tenants would lease the space for less than 10 years. The 470 Noor Ave landlord will deliver the space in a clean vanilla shell at occupancy, provide tenant improvement allowance and allow tenant time to install tenant improvements and fixtures. Email correspondence with Mike Berube discusses tenant improvement allowance and a longer lease period, both requirements for anchor tenants. The Noor property is in close proximity to easy freeway access (HWY 380) and Tanforan, a regional shopping center.

City of South San Francisco

c/o Michael Lappen

re: lease – amended proposal - Pet Club - *comparables*

1 Chestnut Avenue, South San Francisco, Ca

October 9, 2012

page 2 of 2

We include with this letter;

1. Email correspondence with Don Krieger of Terranomics – 9-27-12. (*separate delivery*)
2. Letter from Christine Firstenberg of Metrovation – 10-1-12.
3. Kidder Mathews – 14 comparables – 4 pages – 10-2-12.
4. Email from James Gaglione – Kidder Mathews – re: comp #10 & #12 – 10-5-12.
5. Email from James Gaglione – Kidder Mathews – re: Dollar Tree – 9-28-12.
6. CBRE – 5 comparables – 5 pages.
7. The Berube Company – 470 Noor Ave. comparable w/ email 10-4-12.

The documentation previously submitted or accompanying this letter is provided on behalf of Pet Club and with the understanding that all individual writings are privileged and should only be distributed to necessary parties and unless stated otherwise are to remain confidential.

The Pet Club offers base rent of \$35,890.00 monthly (before TI / Set Up Allowance), a blended base rental rate of \$1.35/sf/mo (\$16.25 annually) NNN. Assuming little or no value to the mezzanine space the effective rent for the ground level space is approximately \$1.67/sf/mo (\$20.00 annually) the higher rent range of retail space. Additionally, approximately \$65,400 or \$5,450 per month from the sales tax revenue should be considered as additional rent payable by Pet Club, adjusting the effective rent to \$41,340.00/month (\$1.56/sf/mo on entire building area or \$1.92/sf/mo on ground floor only space).

As stated in Pet Club's proposal, a lease with Pet Club will generate approximately \$808,012.00 (544,000 + [35,890-13,889-22,001x12= \$264,012] = 808,012) annually (\$67,334 monthly) payable to the State, City and beneficiary agencies or \$2,424,036 over the three (3) year term.

The Pet Club lease proposal of 10-3-12 for 1 Chestnut offers a higher rent, nominal tenant improvement allowance (**paid by tenant not landlord**, but recaptured) and a short lease (3 years), a combined proposal that is more favorable than most of the comparable properties and easily supported by the documentation provided. Upon review we trust you will conclude the rent and other considerations offered by Pet Club are more than fair and equitable for 1 Chestnut.

Please call to discuss should you have questions with the foregoing or any attachment. You can reach me at telephone 650-401-8500 or 650-520-5559

Very truly yours,

Wall Street Properties



Victor M. Catanzaro  
President

DRE 00531029

Cc: Mr. Tom Lee, Pet Club