CITY OF HAYWARD
HEART OF THE BAY

DATE: April 25, 2023

TO: Mayor and City Council

FROM: Director of Public Works

SUBJECT: Airport Rental Rate Adjustment: Adopt a Resolution Amending the FY24 Master Fee Schedule and Adjusting Hayward Executive Airport Hangar Rental Rates

RECOMMENDATION

That the Council adopts a resolution (Attachment II) authorizing an amendment to the FY24 Master Fee Schedule, which would increase monthly Airport hangar rental rates by 8.5%; and implements changes to the Master Fee Schedule for FY24, which would increase monthly rents associated with storage rooms, office spaces, and tiedown spaces by 8.5%.

SUMMARY

The Airport operates as an enterprise fund and relies solely upon the revenue it generates to fund its operating and capital improvement budgets. Accordingly, the Airport does not receive any financial support from the City's General Fund.

Airport staff regularly monitor the operating budget to reduce costs and adjust revenue so that the Airport can remain in good financial health. For example, commercial rents were increased in January of 2023 by the maximum-allowed amount of 7%. Staff has also been successful in applying for and receiving monetary grants from the Federal Aviation Administration (FAA) and California Department of Transportation (Caltrans) to fund capital projects, totaling approximately $3 million over the past ten years. The objective, in conformance with Council directives and FAA standards, is to become and remain financially self-sufficient.

During 2017, a rental rate study was conducted by an independent consultant that determined rental rates were 51% below the market rate. Due to the findings from the study, staff recommended an annual increase of 10% per year over five years. However, after extensive discussions with tenants, an agreement was reached that considered annual increases of 2.5% to 5% per year during the next four fiscal years. On January 15, 2019[1], Council approved a series of annual rental increases for hangar tenants that reflected the revised percentages. Standard-sized hangars increased by 5% annually, and other types of hangars were increased by 2.5%. These increases were implemented over four fiscal years

[1] CITY OF HAYWARD - File #: PH 19-004 (legistar.com)

(from FY19 through FY22). Going forward, staff used objective criteria, past practice, a needs analysis, and current policies to establish new rental rates for FY23:

- Current hangar rental rates at nearby general aviation airports
- The cost of future capital projects to improve infrastructure and enhance safety
- Current and historical Consumer Price Index (CPI) rates for the San Francisco Bay Area (all consumers)

According to the latest data from October, the annual CPI increase for FY23 was 6.0% and 5.3% for FY24 (measured from February 2022 to February 2023). The CPI data was discussed with tenants during two meetings held in February and March. In order to lessen the financial impact to tenants, staff proposes a one-time increase of 8.5% effective July 1, 2023, that takes into consideration 75% of the CPI for FY23 (4.5%) and 75% of the CPI for FY24 (4%). The 4.5% increase for FY23 will not be collected.

In addition to hangar rent increases, Airport staff is also recommending adjustments to the FY24 Master Fee Schedule by 8.5% for hangar storage rooms, office spaces, and tie down spaces.

Discussion with Council Airport Committee and Members of the Hangar Tenant Community

This item was considered at the Council Airport Committee (CAC) meeting of January 26, 2023. While CAC members were generally supportive of the rate adjustments, they requested that Airport staff meet with the tenants to discuss the proposed increases.

On February 22, 2023, Airport staff held an online meeting with tenants to present the proposed rent increases and address questions and concerns. A follow-up meeting was held on March 21 to further discuss the rate increase. Tenants proposed a series of rent increases over the next five years that would vary between 2.3% and 3.0% per year and were tied to the future CPI forecast issued by the White House. However, this proposal is not in conformance with current policies related to CPI increases, which utilize year-over-year actual CPI changes for the San Francisco Bay Area to determine the adjustment
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BACKGROUND

Hangar Rent Increases

The Airport operates as an enterprise fund and relies solely upon the revenue it generates to fund its operating and capital improvement budgets. It does not receive financial support from the City's General Fund. Both the Council and the CAC have expressed a desire to make the Airport as financially self-sufficient as possible. The FAA has a similar policy objective for airports. A key element of self-sufficiency is to reduce costs and increase revenue whenever possible. On the cost side, for example, staff recently replaced a software package with a new one that provides more capabilities at a lower monthly cost, saving approximately $25,000 over the life of the contract.

Staff also work to increase revenue by actively working to lease vacant parcels of land for commercial development, renegotiating existing commercial leases, as well as instituting rental increases for individual and commercial tenants.

A standing City policy for adjusting hangar rates was recommended by the CAC and later adopted by Council. At its meeting on May 25, 1999, a methodology was recommended to and approved by Council to increase rates every other year, on odd numbered years, by 75% of the CPI during the same period. In addition, staff were directed to conduct a market analysis every four years to ensure that hangar rents are consistent with prevailing market rates.

Because of adverse economic conditions and staff oversight, there were occasional deviations from this policy. For example, the last market rate study prior to 2017 was conducted in 2007. This benefited tenants, but it also contributed to widening of the gap between the hangar rents charged at Hayward in comparison with those at other airports in the long run. As a result, rental rates at Hayward did not keep pace, and that in turn created some budget challenges.

In March 2017, a market rate study was completed by an independent firm to determine whether the rents charged for hangar space at Hayward Executive Airport were commensurate with those at other similar airports. The firm identified comparable local airports and airports in other cities across the country. The results indicated that Hayward's rental rates for standard sized hangars were 51% below the market rate, while most other hangar sizes were below the market rate by up to 26%.

The FAA reviewed and supported this approach in a letter dated September 27, 2018.

To arrive at rental rates that would meet the Airport's financial needs and be acceptable to the hangar tenant community, City staff met four separate times with tenants to receive feedback. The net result was realized on January 15, 2019, when Council approved an annual standard sized hangar rent increases of 5% (and all other hangars by 2.5%) from fiscal year 2019 through fiscal year 2022. It should also be noted that Council took action at that meeting to rescind the rent increase policy adopted on May 25, 1999 suspending the use of CPI and rent studies as a basis for rent calculation through the end of FY 2022. However, no recommendation was provided to Council on how to adjust rates after FY 2022. Therefore, staff reviewed prior policies to eventually arrive at an equitable solution for FY 2023 and FY 2024 rent increases that utilized the prior practice of adjusting rates by 75% of CPI.

<u>Master Fee Schedule Updates</u>
In addition to hangars, the Airport rents office space, storage rooms, and outdoor aircraft tie down space. Storage room rental rates were increased in FY 2019, the rates for offices and tiedown spaces now require adjustment to remain competitive.

DISCUSSION

<u>Hangar Rent Increases</u>
As noted earlier, Council approved a four-year series of hangar rent increases in 2019. That series of increases concluded on June 30, 2022. A decision was made to delay future rent increases for the first portion of FY 2023 until Airport staff could review the actual

revenues and expenditures for FY 2022. It was determined that to keep pace with inflation and meet the need for future capital improvements, such as paving and hangar repairs, rental increases are indicated through FY 2024. It should be noted that hangar occupancy rates have remained steady after implementing the prior rent increases and through the COVID-19 pandemic.

Justification
It is important to clarify the reasons for the proposed rental increases and the methodology used for the adjustment. The Airport operates as a financially independent enterprise fund. Through the administration of fees and charges, the Airport finances all its operations including transfers to fund a Capital Improvement Program (CIP). The Airport does not receive revenue from the City's General Fund. The costs incurred to operate the airfield are noted under "expenditures" in the Airport's FY 2023 budget forecast (please refer to Attachment III).

Recent history shows that revenues are not keeping pace with the costs to maintain and manage the Airport. Personnel costs continue to increase due to a rise in retirement and medical costs. In addition, the Airport's yearly contribution to fund its capital improvements continues to increase as construction contracts and associated material (such as asphalt) become more expensive. For FY 2023, the Airport is expected to experience a shortfall of approximately $1.1 million. Balanced budgets are not forecast until FY 2027, but this result is based on revenues from land leases that are currently under negotiation or capital projects that are under review by Council. Future development by commercial tenants will not be assured until negotiations are finalized, bank financing is secured, building permits are issued, and the projects are constructed.

In response, Airport staff has taken steps to reduce costs and improve revenue, such as signing long-term leases for vacant parcels, increasing commercial aeronautical rents by regularly scheduled CPI adjustments as outlined in their lease agreements, actively marketing vacant parcels, and aggressively pursuing federal and state grant opportunities to offset the use of airport funds for capital projects, among other initiatives.

In addition, Airport staff has undertaken several cost cutting measures:

- LED lighting in hangars, which, after the initial investment, reduces electrical consumption and cost.
- Use of infrastructure funding for pavement repairs
- Replacement of the transformer in each runway edge light
- Reducing the number of vehicle gates and associated maintenance
- Use of infrastructure funding for replacement of obsolete equipment, such as the fire alarm system.
- New inspection software, which standardizes inspections

Methodology
Staff reviewed strategies employed in the past to make a recommendation for rental increases. Since an independent rental study was completed less than five years ago, consideration was focused on employing an increase tied to the Consumer Price Index (CPI).

The initial proposal presented to the tenants in February was to increase both FY 2023 and FY 2024 rents by 100% of CPI and to implement the FY 2023 increase on April 1 for the remaining three months of the fiscal year (June 30). However, after two meetings with the tenants, and in response to their feedback, this initial proposal was modified.

The revised proposal recommends that hangar rents be increased by 75% of CPI for both FY 2023 and FY 2024, with a one-time increase for FY 2024 to occur on July 1, 2023. This compromise allows rents to keep relatively close to the pace of inflation, while easing the impact of the rent increase on tenants and not subsidizing one group of airport users with another. In early FY 2024, staff will review the Airport's financial standing to determine what future CPI-related increases are needed, or some other form of rent adjustment would be preferable and present the findings to the CAC and Council. The concept of annual rent increases tied to CPI is used by many of the general aviation airports in the Bay Area, including Reid-Hillview, San Martin, Livermore, Palo Alto, and Buchanan Field.

Additional revenue benefits airport tenants through the completion of capital improvements that enhance safety and efficiency, such as outlined above.

For FY 2024, staff is recommending that the new rates be implemented by July 1, 2023. This time frame includes Council consideration of the item and, if approved, compliance with the following policies:

- Per Administrative Rule 1.21, at least sixty days must pass prior to enacting any revisions to the existing Master Fee Schedule
- Staff is required to notify tenants at least thirty days in advance of the rate change

The CPI for the Bay Area (all urban consumers/all goods) rose by 6% between October 2021 and October 2022, while the CPI to be utilized for FY 2024 rose by 5.3% between February 2022 and February 2023. 75% of the CPI FY 2023 amounts to 4.5% and the FY 2024 increase was 4%. This increase between both fiscal years of 8.5% will be applied to all monthly hangar rental rates at the airport for FY 2024.

In order to moderate this increase to hangar rental rates for FY 2023 and FY 2024 and to lessen the financial impact to tenants, this one-time adjustment will be implemented in July 2024 and not applied retroactively to July 1, 2022. Therefore, tenants were not subject to an increase for FY 2023 and were paying the same rate for two years in a row (FY 2022 and FY23). In addition, tenants will not be subject to the full amount of the CPI in either FY 2023 or FY 2024, which results in an annual savings of $168 from the original proposal of 100% CPI for a standard hangar.

A summary of the rate changes per hangar type is highlighted below and are rounded to the nearest dollar:

Hangar Type	Current Rent/Month	FY 2024 Rent (Effective 7/1/23)	Increase/ Month
Small	$294	$319	$25
Standard	$455	$494	$39
Large	$566	$614	$48
Small Executive	$982	$1,065	$83
Standard Executive	$1,359	$1,475	$116
Large Executive	$1,483	$1,609	$126

Updates to Master Fee Schedule

Each year, Airport staff evaluates other various fees associated with the Master Fee Schedule to ensure they are fair and reasonable in light of existing economic conditions and financial needs of the airport. The last update occurred in FY 2021 and focused on increases to staff costs to perform certain functions, such as ramp sweeping services and hangar cleaning performed by Maintenance staff after tenants vacate.

For FY 2024, staff is recommending changes to several rates by the same increase of 8.5% (rounded to the nearest dollar) that is proposed for the hangars:

- **Hangar storage rooms**

Storage Room Type	Current Rent/Month	FY 2024 Rent (Effective 7/1/23)	Increase/Month
Small	$73	$79	$6
Medium	$101	$110	$9
Large	$196	$213	$17
Extra Large	$250	$271	$21

- **Office spaces**

Current Rent/Month	FY 2024 Rent (Effective 7/1/23)	Increase/Month
$650	$705	$55

- **Tie down spaces**

Current Rent/Month	FY 2024 Rent (Effective 7/1/23)	Increase/Month
$60	$65	$5

ECONOMIC IMPACT

For FY 2024, a standard hangar tenant would pay an additional $39 per month, or $468 annually with the proposed 8.5% adjustment.

FISCAL IMPACT

The rent increase is expected to generate approximately $151,000 in additional revenue in the Airport Fund for FY 2024.

STRATEGIC ROAPMAP

The additional rent generated from the increase will support the Strategic Roadmap to Invest in Infrastructure. Specifically, this item will support the following project:

Invest in City Facilities & Property
N12: Upgrade and maintain Airport infrastructure and facilities
N12a: Rehabilitate the Pavement in Phases
N12b: Design and Construct Capital Improvements to Airport Hangars

SUSTAINABILITY FEATURES

This report does not pertain to any sustainability features.

PUBLIC CONTACT

This item was considered at the CAC meeting on January 26, 2023. While CAC members were supportive, they requested that Airport staff meet with the tenants to discuss the proposed increases.

<u>Discussion with Members of the Hangar Tenant Community</u>
On February 22, 2023, Airport staff conducted an online meeting with tenants (feedback collected was presented to the public at the CAC and in the staff report) to present and explain staff's initial approach to rate adjustments. Thirteen members of the larger tenant group attended the meeting and voiced concerns over using the full CPI to adjust rents. Staff noted that all of the tenant increases since FY 2019 have been reinvested back into the Airport through hangar, lighting, and pavement improvement projects.

On March 21, 2023, staff conducted a follow-up meeting attended by seventeen tenants to present the revised framework for the rent increase, which included utilizing 75% of the Bay Area CPI (all consumers) for both FY 2023 and FY 2024 to arrive at a one-time increase of 8.5% effective July 1, 2023. The tenants were appreciative of the effort staff made to lessen the rate but were still concerned about the size of the increase. The group proposed an alternative rate structure (Table 1 below) that established a series of set increases for the next five years that closely mirrored the future CPI forecast, which is a composite of various predictions and forecasts (see also Attachment IV).

Table 1. Tenant Proposal

Hangar Type	Current Rent/Month	FY 2024 Rent (2.46% Increase)	FY 2025 Rent (2.46% Increase)	FY 2026 Rent (2.46% Increase)	FY 2027 Rent (2.46% Increase)	FY 2028 Rent (2.46% Increase)
Small	$294	$301	$309	$316	$324	$331
Standard	$455	$466	$478	$489	$501	$514
Large	$566	$580	$594	$609	$624	$639
Small Executive	$982	$1,006	$1,031	$1,056	$1,082	$1,109
Standard Executive	$1,359	$1,392	$1,427	$1,472	$1,498	$1,535
Large Executive	$1,483	$1,519	$1,557	$1,595	$1,634	$1,675

The rationale behind this approach was to equate their increases with the rate schedule paid by commercial leaseholders, which allows for actual annual CPIs but capped at a maximum 7% increase every five years. The total increase to the monthly rent from FY 2024 to FY 2028 would be 12.3%, or 2.46% per year. While staff was appreciative of the proposal, they mentioned this would not be feasible as it runs counter to long-standing policy, which utilizes existing CPI data to determine future rent increases. Furthermore, as has occurred during the past year, the CPI can increase in short order, thereby rendering any forecasts invalid for rate setting purposes. In addition, commercial leaseholders are subject to a market rate study every ten years (with the next appraisal scheduled for 2028), which may increase rents by more than the CPI over the same timeframe. Finally, commercial tenants pay for their own utilities and maintenance, while those costs are included as part of the tenants' monthly rent.

A summary of comments from the March 21 meeting and responses from staff to those comments is included in Attachment IV.

A public hearing notice was published in the *Daily Review* on April 14, 2023. In addition, the agenda and staff report for this item have been posted on the City's website and distributed to interested parties.

NEXT STEPS

If approved by Council, the new hangar rates will be effective on July 1, 2023, which exceeds the sixty-day window required under the City's Administrative Rule 1.21 for Master Fee Schedule changes. Pursuant to the adoption of the resolution revising the City's Master Fee Schedule, staff will distribute notices to all Hayward tenants with the heretofore mentioned effective date of July 1, 2023.

Prepared by: Doug McNeeley, Airport Manager

Recommended by: Alex Ameri, Director of Public Works

Approved by:

Kelly McAdoo, City Manager