

#### MEMORANDUM

**Date:** April 14, 2010

**To:** California State Lottery Commission

From: Joan M. Borucki

Director

**Prepared By:** Terry Murphy

Deputy Director, Operations

**Subject:** Item 8(b) – Southern Distribution Warehouse Lease

Amendment

# **ISSUE**

Should the California State Lottery Commission (Commission) approve a lease extension/modification for the Southern Distribution Warehouse (SDW) and acquire new space for the Auxiliary Southern Distribution Warehouse (ASDW) with Laird Properties, LLC through June 30, 2017?

## RECOMMENDATION

Staff recommends the Commission approve a seven-year lease extension for the SDW (\$1,424,304) and add space next door to replace the existing ASDW (\$906,447). The total amount of the lease extension, which includes adjusted payments for the June 15, 2010 – June 30, 2010 period, is \$2,330,751.

## **BACKGROUND**

The California State Lottery (Lottery) leases space known as the SDW and has occupied the current 28,350 square-foot facility located at 9430 Lucas Ranch Road, Rancho Cucamonga, California, since February 27, 1995. The space is undersized but acceptable to the Lottery Facilities Section and Lottery Sales as a distribution warehouse. The existing lease extension is due to expire June 30, 2010. The Lottery and the Lessor, Laird Properties, LLC, have experienced a good working relationship in the past, and it is agreeable to all parties that the Lottery continues to occupy the space.

The Lottery also occupies approximately 12,741 square feet of additional space for the ASDW, located at 11150 Arrow Route, Rancho Cucamonga, California. The existing lease expires June 30, 2010.

Lottery staff has negotiated new terms and reduced rates for the main SDW. The reduced rates are contingent on the Lottery taking on additional space adjacent to the main SDW to use as the auxiliary warehouse.

## **DISCUSSION**

The charts below compare the FY 2010/11 cost of (A) remaining in the SDW and current ASDW for one year and (B) extending the SDW lease for seven years and replacing the current ASDW with property next to the SDW.

# 2010/11 Monthly Costs

A. Extend Current Leases for One Year						
	ASDW	SDW	Total			
Sq. Ft.	12,741	28,350	41,091			
Cost/Sq. Ft.	\$0.45	\$0.66				
+Total Cost	\$5,733.45	\$18,582	\$24,315.45			

B. Extend SDW Lease Seven Years and Add Adjacent Space to Replace ASDW						
	ASDW	SDW	Total			
Sq. Ft.	20,450	28,350	48,800			
Cost/Sq. Ft.	\$0.45	\$0.52				
Total Cost	\$9,202.50	\$14,742	\$23,944.50			

If the SDW lease is extended for seven years and the ASDW moved next door, the Lottery will reduce its southern warehouse lease cost by \$370.95 for FY 2010/11 and gain 7709 square feet of space. The lease extension will provide a lower base rate with modest \$.025 per square-foot annual increases. SDW shipping operations will be able to expand into the ASDW space if needed. Additionally, the adjacent location will improve supervision and eliminate the need to travel three miles each way several times per week.

The estimated cost to move the materials currently housed in the existing auxiliary warehouse to the new space is \$6,500.00. The Lottery will occupy both ASDWs from June 15, 2010 to June 30, 2010 to conduct an orderly transition. The overall lease extension amount has been adjusted to reflect the lower rate for the SDW as of June 15, 2010.

California State Lottery Commission April 14, 2010 Page 3

To ensure the Lottery will be paying market rates, staff performed a market rate analysis of the surrounding properties in the area. The following are examples of rents found in the area that justify the new lease rates:

Property Address	Sq Ft	Rate	CAM Charges*	Sub-total Market Rent
Rancho Tech Park	40-60,000	\$.41	Negotiable	\$.41 +
Archibald Bus. Ctr.	various	\$.48	Negotiable	\$.48 +
10939 Jersey	60,000	\$.45	Negotiable	\$.45 +
8822 Flower	10-16,000	\$.48	Negotiable	\$.48 +
9448 Richard Pl	22,000	\$.49	Negotiable	\$.49 +

Although there is currently "large" space available at or below the rates the Lottery has negotiated, the Lottery has not determined its long-range strategy for the SDW. Also, the cost to move operations, including necessary tenant improvements, telecommunications infra-structure, and special security conditions to which the Lottery must adhere, make it impractical to take advantage of all the market conditions that might otherwise be available. Nevertheless, Lottery staff has been able to negotiate significant reductions in lease rates.

The alternative is to exercise a one-year extension the Lottery has available at the main SDW at \$.66 per square foot and to simultaneously try to negotiate a one-year extension to the ASDW, probably at \$.45 per square foot. This is not recommended as the proposed lease extension gives the Lottery an opportunity to obtain lower rates now and, if necessary, vacate without penalty with 180-days' notice.

\*CAM = Common Area Maintenance charges that may be added to a lease. The Lottery's proposed lease with Laird includes these charges.