



THE CITY OF SAN DIEGO

OFFICE OF THE INDEPENDENT BUDGET ANALYST REPORT

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IBA Review of Proposed SDCCU Stadium Lease Extension with San Diego State University

OVERVIEW

On July 25th, the Smart Growth and Land Use Committee heard an item proposing a new lease amendment for use of the SDCCU Stadium (stadium) with San Diego State University (SDSU). Operation of the stadium currently represents a net cost to the City, with an operating deficit of \$3.3 million projected for FY 2018, and a deficit of \$7.3 million budgeted for FY 2019. At present, the stadium is scheduled to close at the end of this year, and no events at the stadium are currently scheduled after December 31, 2018.

The proposed lease amendment would extend SDSU's lease at the stadium for two years, from December 31, 2018 to December 31, 2020, and increase the City's expected annual revenue at the stadium by \$1.7 million. Approval of the lease amendment would commit the City to operating the stadium for an additional two years.¹

The Committee forwarded the proposed lease to Council without recommendation, requested further clarification on the costs of operating the stadium, and requested that the Real Estate Assets Department (READ) pursue additional negotiations with SDSU before the item is brought to Council. Additionally, on July 20th our office received a memo from Councilmember Sherman that requested further information related to the costs of operating the stadium and potential costs of closing the stadium.

Our office subsequently met with both the Department of Finance and READ to clarify financial projections and further analyze Councilmember and Committee requests. This report includes the information requested by Councilmembers and the Committee.

¹ Should either of the pending Initiatives related to the stadium – Soccer City and/or SDSU West – be approved by voters in the November election, its provisions would supersede this lease and any associated City commitments.

BACKGROUND

Stadium Operations

Operations at the SDCCU stadium are supported by the Stadium Operations Fund. The Fund receives revenue from lease agreements and charges for services, as well as transfers from Transient Occupancy Tax (TOT) receipts, to support required expenditures.

The stadium has hosted NFL and NCAA football games, national and international soccer matches, and concerts, among other events, though stadium operations have historically represented a net cost to the City, which necessitated the TOT transfers. Events scheduled to be held at the stadium in FY 2019 include SDSU football games, soccer games, and concerts. After the Chargers left San Diego in January 2017, the City stopped booking events at the stadium that would take place after December 31, 2018. No events are currently scheduled at the stadium after December 31, 2018.

Proposed Lease with SDSU

SDSU's existing lease at the stadium expires on December 31, 2018 and requires SDSU to pay the City a \$1 per ticket surcharge and to reimburse the City for its game-day expenses. In FY 2018, the City received \$154,000 in revenue from the ticket surcharge and \$667,000 in reimbursements for game-day expenses.

The proposed lease amendment would extend the expiration date of the lease to December 31, 2020, and replace the ticket surcharge with a flat rent of \$1.1 million per year. Additionally, parking and concessions revenue (\$733,000 in FY 2018) which is currently retained by SDSU under the existing lease would instead go to the City. This would increase revenues associated with this lease from \$154,000 per year to \$1.8 million per year during FYs 2020-21.

As the City had planned to begin winding down operations at the stadium in January 2019, approval of the proposed lease extension would delay this wind-down and would commit the City to operating the stadium for an additional two years.

FISCAL AND POLICY DISCUSSION

Revenue and Expense Projections

As noted above, the stadium has historically operated at a deficit.² The FY 2019 Adopted Budget shows a budgeted operating deficit of \$7.3 million.³ The FY 2018 Adopted Budget showed a budgeted operating deficit of \$7.6 million, but actual expenditures and revenues resulted in the deficit experienced by the City being lowered to \$3.3 million, largely due to increased revenues from concerts and other events that total \$6.7 million and that are shown on the table on the following page.

² Questions arose during discussion of this item at the Smart Growth and Land Use Committee as to the actual deficits experienced and projected for FYs 2018-19. After the Committee meeting, our office met with the Department of Finance to reconcile projections, and both offices agree with the FY 2018-19 projections included in this report.

³ These amounts do *not* include debt-service payments on stadium renovation bonds and do *not* include revenues associated with TOT transfers. They consist *solely* of operating expenses and revenue from stadium operations.

READ staff indicates that the \$6.7 million in FY 2018 operating stadium revenue was unusually high and likely represents an outlier year, and that the revenue of \$3.7 million budgeted for FY 2019 represents a more typical year's revenue from stadium operations.

Our revenue projections below for FYs 2020-21 are based on FY 2019 revenue projections, and also include the addition of increased revenue associated with the proposed lease amendment.⁴ Operating Expenditures are assumed to remain constant from FY 2019 on.

Projected Stadium Operating Expenditures & Revenues with Lease Amendment				
	<i>FY 2018</i>	<i>FY 2019</i> <i>(current year)</i>	<i>FY 2020</i>	<i>FY 2021</i>
<i>Revenue</i>	\$ 6,674,214	\$ 3,680,309	\$ 5,372,179	\$ 5,372,179
<i>Expenditures</i>	\$ 9,970,124	\$ 11,011,893	\$ 11,011,893	\$ 11,011,893
<i>Deficit</i>	\$ (3,295,910)	\$ (7,331,584)	\$ (5,639,714)	\$ (5,639,714)

Wind-Down and Decommissioning Cost Assumptions

After the Smart Growth and Land Use Committee, our office met with READ staff to review potential costs that would be associated with winding down operations and decommissioning the stadium. Decommissioning a stadium is not a function the City has performed in the past, and READ's initial research suggests that it could take up to 18 months to wind down operations.

If the lease amendment is not approved and wind-down activities take a full 18 months, wind-down activities would take place during the last half of FY 2019 and all of FY 2020. If the lease amendment is approved, wind-down activities would take place during the last half of FY 2021 and extend through all of FY 2022. In either scenario, wind-down operations would extend through the fiscal year following the last event at the stadium.

However, an 18-month wind-down period relies on conservative assumptions. Many recently shuttered stadiums have been demolished between 6 and 12 months after their last event, which suggests a full wind-down period may not take 18 months. Further, it is not clear that a full year's worth of operating expenditures for the final 12 months of wind-down activities would be necessary. READ indicates that it would engage a stadium decommissioning consultant to prepare actual wind-down and closing plans and costs.

The table on the following page shows potential expenditures during the final year of winding down operations at the stadium, during which no events would be scheduled. The column on the left shows a full year's worth of expenditures that is consistent with full operating costs at the stadium. The column on the right shows potentially reduced costs, including a 50% reduction in

⁴ If READ staff is successful in booking additional events, revenue could increase. However, given that 70% of stadium operating revenue generated each year comes from July through December, and READ's indication that revenue generated in FY 2018 cannot be relied on, our projections do not include revenue from any additional events booked beyond FY 2019 levels.

costs for staff,⁵ supplies, and energy and utilities,⁶ a 25% reduction in costs for contracts,⁷ and the removal of \$48,000 in costs for capital maintenance.

Potential Costs in Final Year of Wind-Down Phase		
	Full Year Expenditures	Reduced Expenditures
Personnel	\$ 3,682,939	\$ 1,841,470
Contracts	\$ 3,965,157	\$ 2,973,868
Energy & Utilities	\$ 2,243,820	\$ 1,121,910
Supplies	\$ 1,040,770	\$ 520,385
Other	\$ 79,207	\$ 31,207
Total	\$ 11,011,893	\$ 6,488,839

This table represents a *very rough* estimate of costs the City might experience during the final year of winding down operations at the stadium, and shows costs ranging from \$6.5 to \$11.0 million. Costs during the final year of wind-down may be lower than \$6.5 million, but they should not *exceed* \$11.0 million; more accurate cost projections would be developed by a decommissioning consultant.

The decision to extend SDSU’s lease at the stadium should not significantly impact actual wind-down costs; extending the lease would instead shift wind-down costs from FY 2020 to FY 2022. At present, there are no plans to demolish the stadium, so ongoing security costs estimated at \$600,000 annually would be required at the conclusion of the wind-down period.

Questions in Councilmember Sherman’s Memo

- 1) What is the annual cost to the City to shutter the stadium?

As discussed above, we estimate that costs to shutter the stadium could total \$6.5 to \$11.0 million over the first year following the last event at the stadium. At the conclusion of a wind-down period costs would be limited mainly to security expenses which are estimated at \$600,000 annually.

- 2) What is the annual cost to the City to operate the stadium for an additional two years, excluding revenue?

Actual operating expenses for FY 2018 are projected at \$10.0 million. Annual operating costs at the stadium are budgeted at \$11.0 million for FY 2019. Total expenditures for two years of additional operations would be \$22.0 million.

⁵ Staffing for a full year’s operations at the stadium consists of 36.00 FTEs and \$3.7 million in expenditures. It is possible that staffing could be reduced during wind-down, or that a full year’s worth of staffing would not be necessary.

⁶ A substantial portion of costs for supplies, energy, and utilities are associated with events held at the stadium. Some energy costs (including power for HVAC) and some utilities would still be required during decommissioning.

⁷ Most contracts in place for cleaning supplies, elevator maintenance, HVAC supplies, and others would still be necessary during wind-down activities, but some may have reduced rates. Costs for a decommissioning consultant would be added.

- 3) Does the City have any events scheduled beyond December 2018 that utilize the stadium (excluding parking lot events)?

No events are currently scheduled beyond December 2018.

The stadium has entered into a tentative agreement to host five 'Alliance of American Football' league games in 2019, but that agreement is contingent on a lease extension for SDSU being approved.

- 4) If the City Council approves the proposed lease amendment, does it cover the annual operating costs of the stadium?

No. Annual operating expenditures are expected to total \$11.0 million. This lease amendment is expected to generate \$1.8 million per year. Revenue from other events is currently budgeted at approximately \$3.6 million.

- a. If it does not, how much would the City be subsidizing annually in order to allow for two additional seasons of collegiate football?

Based on currently budgeted FY 2019 amounts, and assuming increased revenue from the proposed lease amendment, continued operations at the stadium will require \$5.6 million per year of additional support beyond anticipated operating revenues in FYs 2020-21.

- 5) Is the operating deficit under the proposed lease agreement greater than the annual cost to shutter the stadium?

The operating deficit under the first year of the proposed lease amendment is lower than the deficit associated with the first full fiscal year of the stadium being shuttered, but is higher in future fiscal years, as shown on the chart below:

Projected Net Deficits under New Lease vs Immediate Wind-Down (\$ in millions)				
	<i>FY 2020</i>	<i>FY 2021</i>	<i>FY 2022</i>	<i>FY 2023</i>
<i>New Lease</i>	\$ (5.6)	\$ (5.6)	\$ (6.5) to (11.0)*	\$ (0.6)
<i>Immediate Wind-Down</i>	\$ (6.5) to (11.0)*	\$ (0.6)	\$ (0.6)	\$ (0.6)

**As discussed above, wind-down costs are currently unknown. A range of \$6.5 to \$11.0 million is a conservative estimate of potential costs; costs should not exceed \$11.0 million.*

Actual deficits in FYs 2020-21 will depend on the actual events booked at the stadium. This chart assumes that non-SDSU-related revenue and expenditure projections for FY 2019 will remain flat in FY 2020 and FY 2021.

Essentially, continued operation of the stadium for two years will shift the majority of wind-down expenses from FY 2020 to FY 2022.

- 6) Are expenses from the budget line-items such as Energy & Utilities and Supplies considered as part of game-day expenses?

A portion of these expenses is recovered through charges for game-day expenses. In FY 2019, total expenses for Energy & Utilities and Supplies are budgeted at \$3.3 million; in FY 2018, SDSU reimbursed the City for \$667,000 of game-day expenses.

CONCLUSION

SDSU's current lease to use the SDCCU stadium for its football games expires on December 31, 2018, and the City had planned to decommission the stadium beginning in January 2019.

The proposed SDSU lease amendment before Council would allow SDSU to play its 2019 and 2020 seasons at SDCCU stadium and would require the City to continue to operate the stadium for two additional years. In exchange for the two-year extension, SDSU would be required to increase the rent it pays to the City from \$1 per ticket (which generated \$154,000 in FY 2018) to \$1.1 million per year and allow the City to retain all net revenue associated with parking and concessions (\$733,000 in FY 2018). This would increase the total revenue generated from the lease from \$154,000 annually to \$1.8 million annually.

The decision to extend SDSU's lease at the stadium should not significantly impact actual decommissioning and wind-down costs; if the lease extension is approved, these costs (roughly estimated at \$6.5 to \$11.0 million) would be shifted from in FY 2020 to FY 2022.

While the proposed lease extension would generate additional revenue at the stadium, because total revenue from operating the stadium does not cover the stadium's operating costs continued support from the City's TOT receipts would be required. We estimate the stadium's operating deficit during the two additional proposed years would total \$5.6 million annually.

The decision to extend SDSU's lease at the stadium and commit to continued stadium operations is a policy decision for Council. The continued net cost to the City associated with stadium operations should be weighed against the benefits associated with events that would be held at the stadium during the extended term.



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