



CITY OF MORRO BAY CITY COUNCIL AGENDA

The City of Morro Bay provides essential public services and infrastructure to maintain a safe, clean and healthy place for residents and visitors to live, work and play.

NOTICE OF SPECIAL MEETING

**Tuesday, December 11, 2018
Veterans Memorial Hall – 4:30 P.M.
209 Surf St., Morro Bay, CA**

ESTABLISH QUORUM AND CALL TO ORDER

PUBLIC COMMENT FOR ITEMS ON THE AGENDA

SPECIAL MEETING AGENDA ITEMS:

- I. ADOPTION OF RESOLUTION NO. 97-18 APPROVING THE CITY OF MORRO BAY'S SHORT-TERM FISCAL EMERGENCY PLAN; (FINANCE)

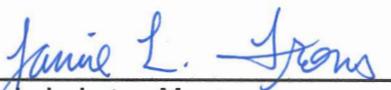
RECOMMENDATION: Council adopt Resolution No. 97-18.

- II. ADOPTION OF RESOLUTION NO. 98-18 APPROVING A NEW MASTER LEASE AGREEMENT BETWEEN THE CITY OF MORRO BAY AND TLC FAMILY ENTERPRISES FOR LEASE SITE 87-88/87W-88W, LOCATED AT 833 EMBARCADERO; (HARBOR)

RECOMMENDATION: Council adopt Resolution No. 98-18.

- III. ADJOURNMENT

DATED: December 6, 2018



Jamie L. Irons, Mayor

THIS AGENDA IS SUBJECT TO AMENDMENT UP TO 24 HOURS PRIOR TO THE DATE AND TIME SET FOR THE MEETING. PLEASE REFER TO THE AGENDA POSTED AT CITY HALL FOR ANY REVISIONS OR CALL THE CLERK'S OFFICE AT 772-6205 FOR FURTHER INFORMATION.

IN COMPLIANCE WITH THE AMERICANS WITH DISABILITIES ACT, IF YOU NEED SPECIAL ASSISTANCE TO PARTICIPATE IN A CITY MEETING, PLEASE CONTACT THE CITY CLERK'S OFFICE AT LEAST 24 HOURS PRIOR TO THE MEETING TO INSURE REASONABLE ARRANGEMENTS CAN BE MADE TO PROVIDE ACCESSIBILITY TO THE MEETING.



AGENDA NO: I

MEETING DATE: December 11, 2018

Staff Report

TO: Honorable Mayor and City Council

DATE: December 4, 2018

FROM: Scott Collins, City Manager
Jennifer Callaway, Finance Director

SUBJECT: Adoption of Resolution No. 97-18 Approving the City of Morro Bay's Short-Term Fiscal Emergency Plan

RECOMMENDATION

Council adopt Resolution No. 97-18, approving the City of Morro Bay's short-term fiscal emergency plan.

BACKGROUND AND DISCUSSION

At the July 10, 2018, City Council meeting, the Council requested a fiscal emergency plan be added to future Council items for Council discussion and decision. In addition, the Council previously requested financial policies be added to a future Council agenda for review and discussion. On August 28, 2018, staff brought forward an action plan outlining the process to complete both a fiscal resiliency plan and formation of Accounting Policies and Procedures. Council approved staff's recommended plan; and staff has proceeded with discussion of fiscal emergency plan, including economic triggers and mitigation measures to be identified in that plan.

The Citizens Finance Advisory Committee (CFAC) received staff's recommended economic triggers on September 18, 2018, and provided feedback on those triggers. On September 25, 2018, the City Council received staff's report regarding the economic triggers and concurred with the five triggers proposed:

1. Natural disaster
2. Human caused Disaster
3. State take-aways of local revenues
4. Large, unexpected costs
5. Economic downturn: (Defined as below)
 - a. Two consecutive quarters of declining revenues in the major revenue's sources identified in the MOUs for COLA increases (sales tax, TOT and Property Tax).

On October 4, 2018, the Employee Budget Advisory Group (Group) met to discuss mitigation measures that would be available for the City Manager and City Council should an economic trigger occur. The Group consists of 14 City employees, representing the various departments and work groups within the City. The Group identified and discussed the following mitigation measures:

1. Hiring Chill – City Manager approval will be required to fill vacant positions. City Manager will only approve filling a vacant position if the Department Director can demonstrate it is

Prepared By: JC

Dept Review: _____

City Manager Review: SC

City Attorney Review: JWP

necessary to meet public health, safety or other high priority service needs that cannot be met on an interim basis through a contract, overtime or temporary staffing. Goal: Short-term savings and preservation of future options should problem be on-going.

2. Travel Chill – City Manager approval for all travel authorizations (at any level). City’s goal is to limit travel and training to achieve short-term savings.
3. CIP Deferrals and or reprioritizations– Department Directors will identify CIP projects that can be presented to Council for possible deferral and/or elimination, as well as reprioritizing capital projects that can be supported in fund other than the general fund.
4. One-Time Operating Cost Review – Identify special projects in the operating budget for possible deferral or elimination (to be presented to City Council for consideration).
5. Fund Balance – Consider use of fund balance below policy levels – City Manager will make recommendation to City Council for consideration.
6. Other – other curtailments as appropriate.

On October 16, 2018, the proposed six mitigation measures were shared with the CFAC with consensus and agreement on the proposed measures. On November 13, 2018, the City Council received staff’s report on the proposed mitigation measures outlined above and generally concurred with them. At that time, City Council provided four comments and direction for change, noting, with respect to the economic downturn trigger, property tax would not fluctuate as much as either sales tax or transient occupancy tax. Based on that, the Council suggested that trigger be clarified to say it will be deemed to occur only two of those identified three major revenue categories trend below expectation for two consecutive quarters. Staff concurs with that recommendation and has added clarifying language.

In addition, City Council provided direction to add a seventh mitigation measure that includes an assessment and determination if the financial condition would warrant transitioning into a long-term recovery and resiliency plan. Staff concurred with that recommendation and provided language to outline this.

Third, the Council directed mitigation measure four above be rephrased to “Operating Cost Review” and include both one-time and ongoing cost review. Lastly, the Council said if an economic trigger occurs and it is deemed fiscal first aid is needed, any review of the fiscal condition and proposed action plan as presented by the City Manager must outline the overall estimated economic impact and proposed target expenditure reduction to mitigate that impact. Language has been incorporated into the draft Fiscal Emergency Plan to address those four directives from Council.

Identification of triggers and mitigation measures is meant to create a transparent process and formula for short-term action when fiscal first aid may be needed. With Council concurrence on the short-term economic triggers and mitigation measures staff has drafted a short-term fiscal emergency plan, provided as Exhibit A to Attachment 1. The short-term fiscal emergency plan will be incorporated into the City’s final overall fiscal resiliency plan which is to be completed during late 2019.

CONCLUSION

Having a clear strategy in place for fiscal emergencies that reflects the City of Morro Bay's values will serve as the foundation for decision-making in tough fiscal times and will aid in preserving the City's long-term fiscal health and vitality. The participation of the Employee Budget Group and CFAC has been invaluable, adding very thoughtful feedback and comments that have been incorporated into the final draft plan. Staff recommends the City Council approve Resolution No. 97-18 adopting the City's Short-Term Fiscal Emergency Plan.

ATTACHMENT

1. Resolution No. 97-18 Adopting the City's Short-Term Fiscal Emergency Plan
 - a. Exhibit A: City of Morro Bay Short-Term Fiscal Emergency Plan

RESOLUTION NO. 97-18

**RESOLUTION OF THE CITY COUNCIL
OF THE CITY OF MORRO BAY, CALIFORNIA,
ADOPTING A SHORT-TERM FISCAL EMERGENCY PLAN**

**THE CITY COUNCIL
City of Morro Bay, California**

WHEREAS, the City Council and staff have identified fiscal sustainability as a core goal and value for the City; and

WHEREAS, in 2015, the City Council hired Management Partners to develop a ten-year financial forecast to help achieve the goal of fiscal sustainability; and

WHEREAS, in 2017/18, the City Council increased fiscal transparency and accountability in the City by providing financial documents on the City's website and implementing the City's online transparency portal, open-gov; and

WHEREAS, in 2018 the City Council has adopted financial and accounting policies, included fund balance reserve levels for the City's General Fund Emergency Reserve, Internal Service Funds, Enterprise Funds and Morro Bay Tourism Business Improvement District Fund, with the goal of providing staff direction and guidance in City practices to ensure the long-term fiscal sustainability of the City; and

WHEREAS, in 2018, the City Council approved the prepayment of the City's Pension Safety Fire Side Fun to reduce overall costs and achieve long-term savings; and

WHEREAS, in 2018, the City Council directed staff to draft a Short-term Fiscal Emergency Plan and Long-term Fiscal Resiliency Plan to prepare the City for future adverse fiscal circumstances that will likely arise in the future; and

WHEREAS, the Fiscal Emergency Plan is meant to provide a transparent and thoughtful action plan, with identified economic triggers and mitigation measures for the City Manager to utilize if fiscal first aid is required; and

WHEREAS, the City's Employee Budget Group and Citizen's Finance Advisory Committee participated in the identification of both economic triggers and mitigation measures outlined in the fiscal emergency plan; and

WHEREAS, staff recommends the City Council adopt the proposed City of Morro Bay Short-Term Fiscal Emergency Plan.

NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Morro Bay, California, the "Short-Term Fiscal Emergency Plan," as set forth in Exhibit A, attached hereto and incorporated herein, is hereby approved.

PASSED AND ADOPTED by the City Council of the City of Morro Bay at a special meeting thereof held on the 11th day of December 2018, by the following vote:

AYES:

NOES:

ABSENT:

ATTEST:

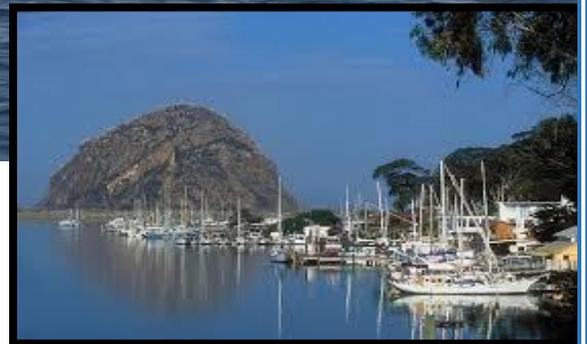
JAMIE L. IRONS, Mayor

DANA SWANSON, City Clerk

CITY OF MORRO BAY



SHORT-TERM FISCAL EMERGENCY PLAN



INTRODUCTION

The City of Morro Bay's FY 2018/19 budget is a reflection of the City's steady growth, particularly in the City's most economically sensitive revenue categories (sales tax, transient occupancy tax). However, with local signs of leveling sales tax growth present coupled with the rising cost to provide services, including rising employee pension costs, the City Council proactively directed staff to develop a Fiscal Resiliency Plan – both a short-term emergency plan and a long-term fiscal sustainability plan. The City's 10-year financial forecast projects a challenging budget forecast ahead, beginning in FY 2019/20 when the PERS discount rate changes will begin to significantly impact the City. The projected impacts are expected to ensue through 2032.

In 2015, the City Council recognized fiscal substitutability as a core goal following the closure of the power plant. The City hired Management Partners to develop a 10-year financial forecasting tool and began to proactively plan for the City's future. The Council has reaffirmed the importance of fiscal sustainability and transparency ever since, by directing staff to develop a fiscal resiliency plan, adopting Accounting and Financial policies and prepaying pension liabilities to reduce interest expense.

While the City's general fund emergency reserves are healthy, at approximately 25% of ongoing expenditures, development in the city remains strong, with permitting fee revenue trending quite well, which cover the City's development costs and provide an overhead revenue source. Despite this period of growth, the City must be ready to weather the next recessionary cycle, which, based on recent sales tax reports, may be in the very near future. Therefore, both short-term and long-term fiscal sustainability must remain at the forefront of budget discussions and considered in all fiscal actions.

The City's fiscal resiliency plan (Plan) is meant to establish a framework and general strategy for responding to adverse fiscal circumstances in both the short term and long term. The Plan does the following:

1. Ensures that employees and the community are meaningfully involved in the process;
2. Takes a policy-based approach to decision-making; and
3. Reflects the City's organizational values.

The Plan is not a specific "recipe" for expenditure cuts or revenue increases, because such measures need to be determined on a case-by-case basis. There are three problems with preparing detailed reduction or revenue options before they are truly needed:

1. If not taken seriously, quality thought will not be given to them;

2. If taken seriously, this is likely to result in needless anxiety in preparing expenditure reductions and sends a conflicting message if times are good; and
3. Even if the preceding points were not constraints, such options would have a short shelf-life, because municipal needs and priorities change over time.

The Plan, rather, articulates the principles and values upon which specific responses will be based.

SHORT-TERM FISCAL EMERGENCY PLAN

The short-term fiscal emergency plan is meant to be an intermediate, quick response to a fiscal emergency. The mitigation measures enacted under the short-term plan are not to exceed 90 days in length while the City Manager assesses the fiscal condition and makes a recommendation to Council for long-term remediation, if necessary. With Council authorization, the short-term mitigation measures may exceed 90 days in length following a full report from the City Manager indicating additional assessment time is needed to determine a long-term fiscal response plan.

TRIGGERS

The short-term fiscal emergency plan is triggered when one or more of the following occur and estimated expenses exceed \$50,000 in the given fiscal year:

1. **Natural disaster**
2. **Human caused disaster**
3. **State take-aways of local revenues**
4. **Large, unexpected costs**
5. **Economic downturn:** Two consecutive quarters of declining revenues in two of the three major revenues sources of sales tax, Transient Occupancy Tax, and property tax. Quarterly reviews will be tied to the City's quarterly budget status report and update which compares quarterly data to prior years same quarters. Declining revenues must occur on a quarter to quarter comparison in two of the three identified revenue categories to trigger a response.

Clearly defining when fiscal first aid is needed is a key factor in the City's ability to successfully take action on a timely basis and avoid worsening the problem.

While the Plan is focused on the City's General Fund, the enterprise funds - water, sewer, Wastewater Treatment Plant and Harbor – also fully participate for two key reasons: (1) we, as a city organization are all part of one team and all parts need to participate; (2) it's important to limit enterprise fund rate increases as much as possible, particularly during recessionary periods and at a time when the City may have to consider other General Fund increases, such as a sales tax increase.

ELEMENTS

The City's Plan comprises five key elements: the minimum fund balance; other key budget and fiscal policies and practices; fiscal health monitoring; assessing whether the situation is a short- or long-term problem; and identifying options.

1. **Minimum Fund Balance:** This is the first line of defense in adverse circumstances. Maintaining the General Fund Emergency Reserve minimum fund balance as 25 percent of on-going annual expenditure, as set by Council policy. That reserve amount allows the City to continue operations and projects, while responding to short-term problems and provides breathing room to address longer-term problems when comprehensive response plans are needed to be developed. That is especially true because Proposition 218 (Prop 218), prohibits the City from imposing new taxes or assessments without taxpayer's approval. For example, Prop 218 and Proposition 26 require (i) majority voter approval for new or increased general taxes, (ii) super majority approval of special taxes, (iii) restricts use of general taxes for general governmental purposes, and (iv) restricts imposition of fees on property owners for services that are available to the public at-large or exceed the actual cost to the City for providing the service.

2. **Other Key Budget and Fiscal Policies and Practices:** Adhering to fiscal policies and practices will help prevent problems at the outset and keep problems from getting bigger when they do happen. The City is in process of developing financial and accounting policies, which include:
 - A balanced budget (and a definition of the term);
 - Conservative investment practices;
 - Diversified revenues;
 - User-fee cost recovery;
 - Enterprise funds;
 - New development paying its own way;
 - Limited use of debt financing;

- Fleet replacement;
- Contracting for services; and
- Productivity improvements.

3. **Fiscal Health Monitoring and Transparency:** During the past 12 months, City Council and staff has worked extensively at enhancing the City’s fiscal health monitoring and transparency. The City has developed and implemented effective ongoing systems for reporting and monitoring its fiscal condition, including interim reporting such as quarterly budget performance status reports, quarterly investment reports, OpenGov on-line transparency portal, a Comprehensive Annual Financial Report, which presents audited financial statements in accordance with generally accepted accounting principles and highest standards. The City uses the following elements as part of its interim reporting:

- An automated financial management system – New World Technologies;
- Online access to the City’s Financial Reporting 24/7 for revenue, expenditure and budget information via the City’s website and OpenGov Transparency portal;
- Bi-Weekly Accounts Payable Registries via the City webpage;
- Quarterly budget status reviews and updates;
- Mid-year budget status review and Capital Improvement Plan review;
- Quarterly investment reports; and
- Monthly reporting of cash and bank reconciliations via the City’s webpage.

4. **Assessing the Situation:** The City uses different strategies for different problems. In the case of a one-time event or downturn that is unlikely to continue indefinitely, one-time fixes are an appropriate response and are considered short-term. However, in the case of ongoing downturns in revenues or systemic increases in costs, one-time fixes won’t work – that type of situation requires new ongoing revenues or ongoing expenditure reductions.

If the assessment concludes the situation is a short-term problem, then the following mitigation measures may be utilized. The mitigation measures may also be utilized during the assessment period. The City Manager has discretion to utilize the following mitigation measures, but to the extent possible will report to the City Council with recommended action prior to implementing any of the identified and agreed to measures below. In times of financial emergency or necessity, when the City Manager implements one or more measures before reporting to the City Council with a recommendation, a complete report of the economic and financial condition that

triggered a response under the short-term plan must be provided to the City Council at the next scheduled Council meeting for ratification or modification as deemed appropriate by a majority of the Council. Under Council direction, the City Manager may be directed to reverse course or implement additional or alternative mitigation measures.

MITIGATION MEASURES

- **Hiring Chill** – City Manager approval will be required to fill vacant positions. City Manager will only approve filling vacant positions if the Department Director can demonstrate that it is necessary to meet public health, safety or other high priority service needs that cannot be met on an interim basis through a contract, overtime or temporary staffing. The goal is to achieve short-term savings and preservation of future options should the fiscal condition be on-going.
- **Travel and Training Chill** – City Manager approval for all travel authorizations (at any level) for training that involves training outside of the County. The City's goal is to limit travel related costs to achieve short-term savings.
- **Capital Improvement Plan (CIP) Deferrals and/or Reprioritizations** – Department Directors will identify CIP projects that can be presented to Council for possible deferral and/or elimination as well as reprioritizing capital projects that can be supported in funds other than the general fund.
- **Operating Cost Review** – Identify special projects and ongoing expenses in the operating budget for possible deferral or elimination. The City Manager will present these projects to the City Council for consideration and direction.
- **Fund Balance** – Consider use of fund balance below policy levels – the City Manager will make a recommendation to the City Council prior to implementing this mitigation measure.
- **Other** – Other curtailments as appropriate and necessary.
- **Assessing the Situation** – The City will likely use different strategies for different problems. For example, in the case of a one-time event or downturn that is not likely to continue indefinitely, one-time fixes are an appropriate response and are considered short-term. However, in the case of ongoing downturns in revenues or systemic increase in costs, one-time fixes won't work – that type of situation requires new ongoing revenues or ongoing expenditures reductions. The City Manager is responsible for assessing the fiscal condition and determining if a transition to a long-term plan is necessary. That will be reported to the City Council within 90 days as outlined below.

When an economic trigger occurs and fiscal first aid is deemed necessary, the City Manager will work within the identified seven mitigation measures above to develop a response plan. The mitigation measures may be implemented singularly or collectively at the City Manager's recommendation and Council direction depending on the extent to which fiscal first aid is needed. Any recommendation and report to the City Council utilizing the Fiscal Emergency Plan as outlined in this document requires an identification of the fiscal condition, forecasted fiscal deficit and corresponding expenditure savings recommended to achieve per the outlined mitigation measures above.

Within 90 days of implementing mitigation measures under this short-term fiscal emergency plan, the City Manager will report back to the City Council with a long-range assessment of the City's fiscal condition. If the assessment determines the fiscal condition is a long-term problem, then the City Manager and Finance Director will prepare a long-term fiscal forecast to define the problem (update to the City's existing 10-year financial forecast with revised revenue and expenditure estimates) and prepare revenue enhancement and expenditure reduction options tailored to the problem defined in the forecast.

Preparing such plans will likely take a minimum of three months. The City Manager is to report to Council on the plan's status and update within 90 days with an understanding that additional time may be needed to finalize the plan. Implementation of an approved plan is likely to take another three to six months. That underscores the importance of a strong fund balance and short-term expenditure reductions to create the time needed to prepare and implement reasonable long-term plans.

5. **Identifying Options:** In the long-term, the solutions are simple – there are only two basic budget-balancing options: Increase Revenues or Reduce Expenditures. In the short-term using fund balance is an option; however it is not a viable long-term solution – strategic use of fund balance to reduce future-year operating costs or increases ongoing revenues may be an acceptable short- and long-term strategy.

EMPLOYEE AND COMMUNITY INVOLVEMENT

Department heads and management staff are responsible for encouraging meaningful employee participation and involvement in preparing to respond to both a short-term fiscal emergency or long-term resiliency plan. For the City's Fiscal Year (FY) 2018/19 budget, an Employee Budget Group (EBG) was formed to review over 400 budget suggestions received

from City employees. Many of these suggestions were incorporated into the City FY 2018/19 budget and many are still being considered and on the “wait” list for staff time to implement.

In development of the short-term plan as defined above, including identifying the triggers and mitigation measures outlined, the City reactivated the EBG to provide feedback and input as to appropriate triggers and measures. In the event that the City will utilize the short-term emergency plan, the City Manager and City Management is committed to open communication and engagement with employees for complete transparency. In the event that a long-term response is needed following the City’s assessment of the financial condition, the City will strive to identify likely position reductions resulting from a long-term plan six months before implementing them in order to be straightforward with affected employees about their employment outlook, provide transfer opportunities and allow affected employees a reasonable amount of time to make other plans.

While operating under a short-term emergency response or transitioning to a long-term response plan, the key values that will guide action under these plans is responsiveness and respect. Treating employees with respect means informing them about City plans that affect them as soon as possible. It also means sharing hard facts and consequences in a forthright and timely way.

The City is also committed to actively soliciting and encouraging meaningful participation by key stakeholders in the budget-balancing process, including the organization as a whole, employee associations and the community. That will require active and ongoing communication.

Sharing fiscal health resiliency planning with the community, the City will utilize a myriad of tools, including the City’s website, City Manager’s update and news releases. City staff may make presentations to interested community groups, and periodic newsletters may be distributed in the City’s utility bills as inserts. The City will update the city’s webpage regularly with information about the process and community forums and workshops that will be held to inform community members and solicit input and work under advisement of the Citizen’s Finance Advisory Committee (CFAC) when possible. Depending on the circumstances, the City may also form an ad hoc advisory community group with a clearly defined role and scope of work.

CONCLUSION

While the specifics of both the process and outcomes change with the circumstances, having a clear strategy in place that reflects the City’s values and serves at the foundation for decision-

making in tough fiscal times will play a key role in preserving the City's organization vitality and fiscal health. Continued monitoring of the results of any action plan in achieving its goal and reporting back to the City Council, community and staff with respect to the City's fiscal condition is a vital component of implementation of either a short-term or long-term fiscal plan. It will be the responsibility of the City Manager, in conjunction with the City's Finance staff to closely monitor the action plan to ensure it is achieving its goals and quickly report any significant deviations to the City Council for action.



AGENDA NO: II

MEETING DATE: December 11, 2018

Staff Report

TO: Honorable Mayor and City Council

DATE: December 6, 2018

FROM: Eric Endersby, Harbor Director

SUBJECT: Adoption of Resolution No. 98-18 Approving a New Master Lease Agreement Between the City of Morro Bay and TLC Family Enterprises for Lease Site 87-88/87W-88W, Located at 833 Embarcadero

RECOMMENDATION

Staff recommend the City Council adopt Resolution No. 98-18, approving a new Master Lease Agreement for Lease Site 87-88/87W-88W, as proposed.

ALTERNATIVES

Council may elect not to approve Resolution No. 98-18 for the new Master Lease Agreement (MLA) as-proposed, and direct staff accordingly.

FISCAL IMPACT

Under this proposal, revenues to the Harbor Fund will remain at the level they were under the previous master lessee at \$30,000/year until the proposed site redevelopment project is completed, then increase moderately at first and eventually after two years reach the \$80,000-\$90,000/year level as the new restaurant, hotel rooms and retail units reach stabilization over that time, coinciding with the initial proposed percent rent concessions expiring.

In addition, assuming the lease concession for hotel valet parking is implemented as-proposed, the revenues from this site could experience a temporary decrease up to \$25,000 maximum per year for up to five years, in the form of a credit against the annual rent on this site. Even with the valet and other concessions, however, overall revenues from this site will increase significantly over historic levels once the redevelopment is complete.

Under this proposal, the General Fund should see an initial increase in Transient Occupancy Tax of approximately \$40,000/year, and an initial increase in Tourism Business Improvement District revenues of approximately \$12,000/year, if the new hotel rooms perform, as anticipated. In addition, the General Fund will receive (\$3,410.00) annually for eight parking spaces proposed to being leased by the tenant in the City's public parking lot at Pacific Street and Market Avenue.

BACKGROUND

The lease for Lease Site 87-88/87W-88W (Lease Site) expired on March 31, 2018. In August 2017, TLC Family Enterprises (TLC) was granted Consent of Landowner (COL) authority to redevelop the Lease Site through a request for proposals process. The COL contains certain "milestones" or timeline performance requirements TLC was to meet to maintain its validity.

In addition to the COL, on April 24, 2018, the Council approved an Interim Lease Agreement with

Prepared By: EE

Dept Review: EE

City Manager Review: _____

City Attorney Review: _____

TLC to occupy and manage the Lease Site during the planning and permitting process, ultimately to be replaced by a long-term MLA once Concept Plan approval was obtained.

To date, all timeline milestone requirements have been met, including obtaining Concept Plan approval from the Planning Commission and City Council. The next major milestone is December 11, 2018, whereby TLC must have a new MLA approved.

Over the past several months, staff and TLC have negotiated a new MLA for the Lease Site to enable its redevelopment, including taking negotiations to the Council in closed session for input and direction.

DISCUSSION

The proposed new MLA with TLC, included with this staff report as Attachment #1 and based on the City's standard lease template, contains the following significant highlights:

1. Section 1.01 Term: 50-year lease term commencing December 11, 2018 based on a minimum \$3.6M investment in the proposed project, and expiring November 30, 2068. That term is commensurate with the degree of investment in and commitment to the project.
2. Section 2.01 Minimum Rent: annual minimum rent, as under the previous master lessee, of \$30,000/year, and subject to standard annual CPI adjustments and five-year reappraisals. Minimum annual rent will be based on the higher of 8% of the appraised value of the property or 75% of the average last five years of total rent paid.
3. Section 2.04 Percentage Rent: all percent rents to be 2% until two years after certificate of occupancy for the redevelopment project is issued, then reverting to 3% for all restaurant sales and beer and wine sales at the bar, 5% for all retail, hotel and convenience/take-out food (yoghurt window) sales, and 10% for all slip revenues and liquor sales at the bar.

The percent rent concessions are commensurate with other comparable lease redevelopment projects to enable new tenants and/or operations to "get off the ground" with some modest and reasonable rent relief. They are also commensurate in scale with the percent rent assumptions in TLC's business plan pro forma years 1-5.

4. Section 3.01 Permitted Uses: permitted uses will be consistent with the property entitlements, namely, restaurant/bar, convenience/take-out food, retail, transient occupancy (hotel) and vessel accommodation.
5. Section 13.01 Tenant's Obligation to Redevelop Site: memorialization of the approved Concept Plan for Lease Site redevelopment, including timeline performance parameters and minimum investment (expenditure) requirements for the project.

Because Concept Plan approval by the Planning Commission was delayed 39 days by no fault of TLC, 39 days have been added to all original COL timelines in this section.

In addition, the deadline by which TLC must show evidence of sufficient financing for the project was changed from April 10, 2019 to August 1, 2019. That change is because, in April, the project will understandably not have reached a point in the permitting process to be far enough along for lending institutions to make any more commitment than TLC has now, which are "letters of interest." By August, the project should be sufficiently defined and

permitted to allow a lending institution to perform an appraisal on the project and property and provide a more definite financial commitment.

Section 13.04 Valet Parking Rent Credit and Hotel Parking Spaces: because the Lease Site has no on-site parking for hotel guests, the MLA includes a rent credit in the amount necessary to offset the actual, documented valet costs necessary for hotel operations, up to a maximum of \$25,000 annually (50% of what is estimated at the high end of what a valet parking program could cost on the waterfront), and offset by any valet parking revenues charged by the tenant. Because the additional estimated annual cost of \$45,000-\$50,000 for a valet system is a significant financial burden for one small 8-room hotel to shoulder, a City incentive (rent credit) is necessary and justified to ensure the project's viability and success.

This credit will be subject to annual review and has a phase-out or sunset clause based on (i) review and determination by the City the credit is no longer needed or justified, or (ii) five years, whichever occurs first.

By way of a separate lease or license agreement for hotel customers from the Lease Site to use up to eight parking spaces in the City's public parking lot at Market and Pacific Streets, between the hours of 3:00 p.m. and 11:00 a.m., for \$3,410.00/year. Those valet and parking provisions are commensurate with lease terms recently granted Doug Redican for his hotel room conversion at Rose's Landing.

CONCLUSION

TLC has operated the Lease Site, as master leaseholder, since April 2018; and although unable to secure a tenant for the defunct restaurant space, in that time has managed the Lease Site in a clean and orderly fashion with Under the Sea Gallery as the prime retail tenant, while continuing to execute elements of the subject redevelopment proposal. As such, TLC is currently a lessee in good standing with regard to ownership and operation of the Lease Site.

The redevelopment will significantly upgrade the Lease Site, bringing it up to modern code standards and creating enhanced public benefits, while increasing revenues for both the Harbor and General Funds due to the increase and mix of uses and LEED certification. As such, staff recommend the City Council approve Resolution No. 98-18, included with this staff report as Attachment #2, approving a new MLA for the Lease Site, as-proposed.

ATTACHMENTS

1. New Master Lease Agreement for Lease Site 87-88/87W-88W.
2. Resolution No. 98-18.

L E A S E

by and between

the CITY OF MORRO BAY

("CITY")

and

TLC FAMILY ENTERPRISES

("TENANT")

L E A S E

This LEASE is made and entered into by and between the CITY OF MORRO BAY, a municipal corporation of the State of California herein called CITY, and TLC Family Enterprises, Inc., a California corporation, herein called TENANT (CITY and TENANT are sometimes collectively referred to as the Parties and individually as the Party).

WITNESSETH

WHEREAS, the State of California granted certain tide and submerged lands located within the CITY limits of CITY to the County of San Luis Obispo and to its successors, being Chapter 1076, Statutes of 1947, as amended by Chapter 413, Statutes of 1955, Chapter 1874, Statutes of 1957, and Chapter 70, Statutes of 1960, first extraordinary session; which Statutes may be amended from time to time by the Legislature of the State of California; all of which Statutes are expressly recognized and agreed to be in full force and effect by the parties hereto; and

WHEREAS, the parties hereto recognize and agree on July 17, 1964, CITY, Lessor herein, succeeded to all of the right, title and interest of the County of San Luis Obispo in and to all of the tide and submerged lands conveyed to said County by the State of California pursuant to the above-mentioned acts; and

WHEREAS, judgment has been entered on October 14, 1968, in the case of CITY, Plaintiff, versus County of San Luis Obispo, and State of California, Defendants, by the Superior Court of the State of California in and for the County of San Luis Obispo, #30417, adjudging and decreeing, among other things, that the title to said tide and submerged lands so conveyed by the State of California to the County of San Luis Obispo in trust, as set forth above, passed automatically to CITY upon the date of its incorporation as a CITY on the 17th day of July, 1964; and

WHEREAS, TENANT accepts the within Lease with full knowledge that there is no warranty of title in and to the within described premises by CITY to TENANT; and

WHEREAS, in order to develop and improve Morro Bay Harbor and to assist in carrying out the provisions of the tideland grant as aforesaid, and in order to provide facilities for the accommodation of those using Morro Bay Harbor, CITY desires to lease to TENANT the within described property upon the terms and conditions set forth herein;

NOW, THEREFORE, in consideration of the covenants to be performed and the rental to be paid by TENANT to CITY, CITY leases to TENANT, and TENANT leases from CITY, all of the following premises (herein collectively referred to as the "Premises") in the City of Morro Bay, County of San Luis Obispo, State of California, described as follows:

Lease Site 87-88/87W-88W

This property is delineated on Parcel Map of the City of Morro Bay No. 68-30, which map was recorded on October 10, 1968, in Book 3, Page 10 of Parcel Maps in the Office of the County Recorder, San Luis Obispo County, California. A copy of said Map is attached hereto as Exhibit A and made a part hereof by reference.

Article 1 FIXED TERM

Section 1.01 Term.

The term of this Lease shall be a period of 50 years, commencing December 11, 2018 (the "Commencement Date"). The term of this Lease shall terminate without notice on November 30, 2068, unless sooner terminated as herein provided.

Section 1.02 No Extensions.

The term of this Lease shall not be extended nor shall this Lease be renewed. Requests for continued use of the Premises shall be treated as an application for a new lease and shall require appropriate application to CITY with all required supporting information and documents, CITY Council approval and the execution of a new CITY lease, containing the then most current terms, covenants, conditions and rent schedules.

Section 1.03 Hold Over.

If TENANT holds the demised Premises after the expiration of the term of this Lease with the consent of the CITY, express or implied, then such holding over (in the absence of a written agreement between CITY and TENANT with respect thereto) shall be deemed to create a tenancy from month to month, terminable on 30-days' written notice from either party to the other, at a monthly rental equal to two hundred percent (200%) of the average total Rent per month for the twelve (12) months immediately preceding the expiration of the Lease, and otherwise subject to each and every term, covenant and condition of this Lease.

Section 1.04 Replacement.

Subject to the next paragraph, as of the Commencement Date, this Lease shall extinguish and replace every prior lease between CITY and TENANT respecting the Premises, if any. Any right or interest held by the TENANT pursuant to any existing lease with respect to the Premises, which is not granted pursuant to this Lease, shall be extinguished as of the Commencement Date of this Lease.

If on or before August 1, 2019, TENANT does not provide satisfactory evidence, as approved by CITY'S Harbor Director, Finance Director and City Attorney, TENANT has obtained all the conditional or other financing necessary to commence and complete the Project (as defined in Section 13.02), then (i) this Lease shall automatically terminate, without any notice to TENANT, and be of no force and effect and (ii) the interim lease between CITY and TENANT for the Premises that was in effect prior to this Lease (a copy of which is attached hereto as Exhibit C) shall be reinstated and remain in full force and effect subject to all of that lease's terms and conditions.

Article 2 RENT

Section 2.01 Annual Minimum Rent.

TENANT agrees to pay to CITY a minimum guaranteed annual rental for the use and occupancy of the Premises, in an initial amount of \$30,000 per year (the "Minimum Rent"), payable in advance in equal semiannual installments on January 1 and July 1 each year during the term of the Lease. If the Commencement Date is other than January 1 or July 1, then TENANT shall pay, on the Commencement Date, the proportionate amount of the Minimum Rent payable for the period from the Commencement Date until the next payment date of January 1 or July 1, as the case may be. If the term of the Lease expires on a date other than December 31 or June 30, then TENANT'S final installment of Minimum Rent shall be proportionate to the time remaining in the term. All Rent, including the Minimum Rent and the Percentage Rent, shall be paid in lawful money of the United States of America, without offset or deduction and shall be paid to CITY at City Hall located at 595 Harbor Street, Morro Bay, California, or at such other place or places CITY may from time to time designate by written notice delivered to TENANT.

Section 2.02 CPI Adjustment to Annual Minimum Rent.

(1) The parties agree, as of every July 1 following the Commencement Date (each, a "CPI Adjustment Date"), except as outlined in section 2.03 hereof, the annual Minimum Rent

shall be adjusted in direct proportion to any upward or downward movement in the Consumer Price Index for January 1, 2018, which is hereby agreed to be 261.235 (Base Index). The percentage adjustment for any given year shall be based on the monthly average Index for the calendar year immediately preceding the CPI Adjustment Date as compared with the Base Index. The Consumer Price Index referred to herein is the Consumer Price Index (all items indexes, all urban consumers) for Los Angeles – Long Beach – Anaheim, California, compiled and published by the United States Department of Labor, Bureau of Labor Statistics, 1982-84 Base Year = 100 (the "Index")

(2) The Annual Minimum Rent shall be adjusted as of each CPI Adjustment Date, and will remain in effect as adjusted until the next CPI Adjustment Date. As an illustration only, if the Base Index (Jan. 1, 1999 CPI) is 166.1 and the monthly average CPI for 2000 is 171.6, then the percentage increase is equal to 3.31%. Therefore, the Minimum Rent would be increased by 3.31% as of July 1, 2001, and would continue at that rate through June 30, 2002.

(3) If the United States Department of Labor, Bureau of Labor Statistics, shall cease to compile and make public the Index as now constituted and issued, but shall substitute another index in its place, then said substituted index shall be used for the purpose of adjusting the Minimum Rent for the Premises. If the Index is changed so that the base year differs from that in effect on the Lease Commencement Date, the Index shall be converted in accordance with the conversion factor published by the United States Department of Labor, Bureau of Labor Statistics.

Section 2.03 Calculation of New Minimum Rent.

At the end of the initial five (5) years and of each five-year period thereafter, a new Minimum Rent shall be calculated for the following five (5) year period (each, a "Subsequent Rental Period") as follows:

A. The Minimum Rent shall be subject to adjustment by appraisal as of the fifth anniversary of the Commencement Date and every five years thereafter (each, an "Appraisal Adjustment Date"). CITY, at its own cost and expense, shall retain an independent qualified appraiser for determination of the fair market value of said premises. Not more than nine (9) months prior to each Appraisal Adjustment Date, CITY shall provide written notice to TENANT of the pending appraisal and the appraiser selected by the CITY to determine the fair market value of the Premises, excluding fixtures and improvements unless such are expressly included in the description of the leasehold hereinabove. If TENANT does not reject CITY's appraiser in writing and within thirty (30) days after CITY's notice of its determination, then the Minimum

Rent for the Subsequent Rental Period shall be in the amount determined by CITY as outlined in this Section 2.03. If TENANT rejects CITY's appraiser within thirty (30) days following CITY's notice to TENANT, then within fifteen (15) days after such 30-day period, each party, at its own cost, shall select an independent professionally designated appraiser who is a member of the American Institute of Real Estate Appraisers, or the Society of Real Estate Appraisers with a designation of MAI (Member of American Institute), SRPA (Senior Real Estate Analysis), to appraise the fair market value of the Premises. CITY may rely on its original appraisal, or select a new appraiser, at its cost. If a party does not appoint an appraiser within fifteen (15) days after the other party has given notice of the name of its appraiser, then the single appraiser appointed shall be the sole appraiser. Each appraiser shall conduct an independent appraisal within thirty (30) days after appointment. If the parties are unable to agree on the Minimum Rent for the Subsequent Rental Period within thirty (30) days after receiving the appraisal(s), then each party shall select one member of a three-member committee. The two so selected members shall select the third member, and this committee shall by majority vote select one or the other of the appraisals. The Minimum Rent determined on the basis of the selected appraisal shall be final and binding and all costs associated with the three-member committee shall be paid equally by CITY and TENANT.

B. In the event the appraisal process is not concluded on or before the Appraisal Adjustment Date, the Minimum Rent shall be adjusted retroactively to such Appraisal Adjustment Date as set out hereinbelow when said appraisal process is completed.

C. The total Rent payable, including both the Minimum Rent and the Percentage Rent for each year within the applicable previous five-year period, shall be averaged to produce the average annual total Rent payable for such previous period.

D. The new Minimum Rent for the five-year period commencing on each Appraisal Adjustment Date shall be the greater amount of seventy five percent (75%) of the average of the total yearly Rent payable during the previous five-year period (as set out in paragraph C. above) or eight percent (8%) of the fair market value of the Premises (as established in paragraph A. above.) The new Minimum Rent shall be divided by two to determine the semiannual payments and shall be paid by TENANT to CITY on the first of each January and July thereafter, or paid monthly at the option of TENANT. This new Minimum Rent shall be adjusted each following year in proportion to any increase in the Consumer Price Index as set out in Section 2.02 of this Lease. The Base Index shall be adjusted upon each Calculation of new Minimum Rent as set out in this section so that the Base Index for CPI adjustment shall be the Consumer Price Index for January 1 of the year of the calculation of new Minimum Rent.

Section 2.04 Percentage Rent.

A. In addition to the Minimum Rent, TENANT agrees to pay to CITY at the time and in the manner hereinafter specified, as additional Rent for the use and occupancy of the Premises, a sum equal to the following for all TENANT'S Gross Sales as hereinafter defined: (i) two percent (2%) for all gross sales as defined until seven hundred thirty days (two years) after the Project as defined in Section 13.02 is entitled to be issued a certificate of occupancy, whereafter it shall be (ii) five percent (5%) for all retail sales, transient occupancy (hotel) use and convenience/take-out food sales; (iii) three percent (3%) for all restaurant sales and beer and wine sales at the bar; (iv) ten percent (10%) for vessel slip and tie-up fees and liquor sales at the bar, and (v) five percent (5%) for all other sales, less the amount of the Minimum Rent paid pursuant to this Lease (the "Percentage Rent").

B. The term "Gross Sales," as used herein, shall mean (subject to the exceptions and authorized deductions as hereinafter set forth), the total selling price and the total gross amount received by TENANT from all rentals, merchandise sold and services rendered in, on or from the Premises by TENANT, its sublessees, licensees, or concessionaires, both for cash and on credit including, but not limited to, rentals of dockage space, leasing and servicing operations and ticket sales, and if on credit whether or not payment be actually made therefore, all charges for services, alterations or repairs made in or upon the Premises; the gross amount received by TENANT for merchandise sold pursuant to orders received in the Premises, though filled elsewhere; and the gross amount received by TENANT from any and all other sources of income derived from the business conducted upon the Premises.

C. Notwithstanding the other provisions of Section 2.04, the term "Gross Sales" shall not include the following items, and such items may be deducted from Gross Sales to the extent they have been included therein or have been included in a prior computation of Gross Sales or for which a Percentage Rent has been paid under this Lease to CITY:

- (1) Credits and refunds made to customers for merchandise returned or exchanged;
- (2) Any sales or excise taxes otherwise includable in Gross Sales as defined in this Section because such taxes are part of the total selling price of merchandise or services rendered in, from, or on the Premises, where TENANT must account for and remit the taxes to the government entity or entities by which they are imposed; and
- (3) With respect to credit card sales, fees retained or withheld by the issuer and/or merchant bank pursuant to TENANT'S credit card acceptance agreement, and
- (4) Rental payments to TENANT from sublessees whose total gross sales are included in gross sales computations.

D. TENANT shall keep or cause to be kept full, complete, and accurate records, and books of account in accordance with accepted accounting practices showing the total amount of Gross Sales, as defined herein, made each calendar month in, on or from the Premises. TENANT shall keep said records and books of account within San Luis Obispo County and shall notify CITY in advance of their location at all times. Furthermore, TENANT shall at the time of sale and in the presence of the customer cause the full selling price of each piece of merchandise, each rental received and each service rendered in, on or from the Premises to be recorded in a cash register or cash registers that have cumulative totals and are sealed in accordance with standard commercial practices. Said records, books of account and cash register tapes, including any sales tax reports that TENANT may be required to furnish any government or governmental agency shall at all reasonable times be open to the inspection of CITY, CITY'S auditor, or other authorized representative or agent of CITY. TENANT consents to the release of sales tax information to CITY and on demand will furnish to CITY a copy of the sales tax reports, quarterly reports and any audit reports of sales for confidential internal use of the CITY in determining Gross Sales for TENANT. TENANT consents and authorizes CITY to request such information directly from the State Board of Equalization or other state agency with which sales tax information is filed.

E. By July 31 of each year, TENANT shall furnish CITY with a statement, to be certified by TENANT as current, true and accurate, which shall set forth the Gross Sales of each department, sublessee, licensee and concession operating in, on or from the Premises for the previous twelve (12) calendar months, ending June 30, just concluded, and the authorized deductions, if any, therefrom; and with it TENANT shall pay to CITY the amount of the Percentage Rent which is due to CITY as shown thereby. If TENANT shall at any time cause an audit of sales of TENANT'S business to be made by a public accountant, then TENANT shall furnish CITY with a copy of said audit without cost or expense to CITY. CITY may, once in any twelve-month period, cause an audit of the business of TENANT to be made by a public accountant of CITY'S own selection. TENANT shall, upon receiving written notice of CITY'S desire for such an audit deliver and make available all such books, records and cash register tapes to the public or certified public accountant selected by CITY. Furthermore, TENANT shall promptly on demand reimburse CITY for the full cost and expense of said audit, should the audit disclose that the questioned statement or statements understated Gross Sales by five percent (5%) or more but less than ten percent (10%). In the event that an audit performed at CITY'S request discloses that TENANT understated Gross Sales by less than 5%, the cost of such audit shall be paid by CITY. In the event any audit or other review of records discloses that the amounts reported as Gross Sales was understated by TENANT by ten percent (10%) or more, CITY shall not only be entitled to recover from TENANT all costs of audit and review, but shall also be

entitled to recover from TENANT a penalty equal to two times the Percentage Rent due pursuant to this Lease on such unreported amounts. Whenever any audit discloses that Gross Sales were understated by any amount, TENANT shall immediately pay the additional Percentage Rent therein shown to be payable by TENANT to CITY, together with interest at the Default Rate thereon, from the date the Percentage Rent was payable until the date paid.

F. CITY shall be entitled at any time within five (5) years after the receipt of any such Percentage Rent payment, to question the sufficiency of the amount thereof and/or the accuracy of the statement or statements furnished by TENANT to justify the same. For the purpose of enabling CITY to check the accuracy of any such statement or statements, TENANT shall for said period of five (5) years after submission to CITY of any such statement keep all of TENANT'S records, including sales tax returns, all cash register tapes and other data which in any way bear upon or are required to establish in detail TENANT'S Gross Sales and any authorized deductions therefrom as shown by any such statements and shall upon request make the same available to CITY for examination.

Section 2.05 Reimbursements.

If TENANT fails to perform any term or covenant of this Lease, then CITY may, but is not obligated to, perform such term or covenant, and TENANT shall reimburse CITY therefore as additional Rent hereunder. As an illustration and not as a limitation, if TENANT fails to procure the insurance required by this Lease, then CITY may, but is not obligated to, obtain such insurance, with the cost of the premiums being due to CITY upon demand as additional Rent.

Section 2.06 Penalty and Interest.

(1) If any Rent is not received within ten (10) days following the date on which the Rent first became due, then TENANT shall pay a late penalty of ten percent (10%) of the amount of the Rent in addition to the Rent.

(2) In addition to the penalty, TENANT shall pay interest at the rate of one percent (1%) per month or fraction thereof or the maximum amount permitted by law as of the date this Lease is signed, whichever is greater (the "Default Rate"), on the amount of the Rent, exclusive of the penalty, from the date on which Rent first became delinquent until paid. The term "Rent" includes any sums advanced by the CITY and any unpaid amounts due from TENANT to the CITY.

Article 3 USE OF PREMISES

Section 3.01 Permitted Uses.

The Premises shall, during the term of this Lease, be used for the purpose of operating and conducting thereon and therein the uses permitted by, and in compliance with, Conditional Use Permit No. UPO-509, as it may be amended from time to time, and for no other purpose. At the Commencement Date, such uses include mixed-use retail, bar and restaurant, transient occupancy (hotel), convenience food and vessel slips/tie-up.

Section 3.02 Unauthorized Use.

TENANT agrees to allow only those uses authorized in Section 3.01, hereinabove and any unauthorized use thereof shall constitute a breach of this Lease and shall, at the option of CITY, terminate this Lease.

Section 3.03 Operation of Business - Hours of Operation.

Failure to actively and diligently conduct the business authorized herein constitutes a breach of the agreement and shall, at the option of CITY, terminate this lease.

(1) TENANT shall during the term of this Lease conduct business of the nature specified in Section 3.01 of this Lease on the Premises in an efficient and diligent manner and keep the Premises open for the conduct of business continuously and without interruption for at least six hours each day of the year except one day each week and legal holidays. This provision shall not apply if the Premises shall be closed and the business of TENANT is temporarily shut down for a period not to exceed fourteen (14) calendar days in any calendar year to make necessary repairs, maintenance or other construction deemed necessary by TENANT. This provision shall not apply if the Premises shall be closed and the business of TENANT is temporarily shut down as authorized or required by the CITY Manager or on account of strikes, walkouts, or causes beyond the control of TENANT or for not more than three (3) days out of respect to the memory of an officer, employee, or close relative of any officer or employee of TENANT.

(2) TENANT shall operate TENANT'S business on the Premises with due diligence and efficiency and in like manner as comparable businesses operated in the CITY or the coastal area of San Luis Obispo County, so as to produce the maximum amount of Gross Sales and gross receipts from services which may be produced from TENANT'S business; and TENANT at all times shall carry on Premises, a stock or merchandise of such size, character, and quality as is reasonable, designed to produce the maximum return to TENANT, when the sale of merchandise is a permitted use under this Lease.

Section 3.04 Competition.

During the term of this Lease, TENANT shall not directly nor indirectly acquire or establish any similar or competing business within a radius of five (5) miles from the location of the Premises, provided, however, that TENANT may, with prior written approval from CITY, own or operate more than one business, whether or not competing and similar along the Embarcadero upon CITY lease sites. The purpose of this section is to prevent and prohibit TENANT from reducing revenue to CITY by diverting business from the operation at the Premises to another similar business owned by TENANT within the CITY but not upon a CITY lease site from which CITY is paid rent based on Gross Sales.

Section 3.05 Hazardous Materials.

(1) TENANT shall not transport, use, store, maintain, generate, dispose, release, treat or discharge any "Hazardous Material" (as defined below) upon or about the Premises (such activities being hereafter referred to as "Hazardous Materials Activities"), nor permit TENANT'S employees, agents, or contractors to engage in Hazardous Materials Activities upon or about the Premises, except as allowed by applicable law. The term "Hazardous Material" for purposes hereof shall mean any chemical, substance, material or waste or component thereof which is now or hereafter listed, defined or regulated as a hazardous or toxic chemical, substance, material or waste or component thereof by any federal, state or local governing or regulatory body having jurisdiction, or which would trigger any employee or community "right-to-know" requirements adopted by any such body. All Hazardous Materials Activities at the Premises shall be conducted strictly in accordance with all applicable laws and regulations. If TENANT shall transport any hazardous waste from the Premises, such transportation shall be done only by a contractor duly licensed to haul hazardous waste and shall use only a duly licensed disposal site approved by TENANT'S liability insurer.

(2) TENANT shall promptly notify CITY of: (i) any enforcement, cleanup or other regulatory action taken or threatened by any governmental or regulatory authority with respect to the presence of any Hazardous Material on the Premises or the migration thereof from or to other property, (ii) any demands or claims made or threatened by any party against TENANT or the Premises relating to any loss or injury resulting from any Hazardous Material on or from the Premises, and (iii) any matters where TENANT is required by applicable law to give a notice to any governmental or regulatory authority respecting any Hazardous Material on the Premises. CITY shall have the right (but not the obligation) to inspect the Premises, to take such remedial action on the Premises, as CITY may deem appropriate, and to join and participate, as a party, in

any legal proceedings or actions affecting the Premises initiated in connection with any environmental, health or safety law.

(3) If any Hazardous Material is released, discharged or disposed of by TENANT or its employees, agents or contractors, on or about the Premises in violation of the foregoing provisions, then TENANT shall immediately notify CITY. CITY may elect either to take such remedial action as CITY deems appropriate, in which event TENANT shall reimburse CITY for all costs thereof within ten (10) days after demand, or direct TENANT to perform such remediation. If CITY directs TENANT to perform the remediation, then TENANT shall immediately take such remedial action, as CITY shall direct. TENANT shall, properly and in compliance with applicable laws clean up and remove the Hazardous Material from the Premises and any other affected property at TENANT'S expense. If CITY directs TENANT to perform remediation hereunder and if TENANT shall fail to comply with the provisions of this Section within five (5) days after written notice by CITY, or such shorter time as may be required by applicable law or in order to minimize any hazard to persons or property, then CITY may (but shall not be obligated to) arrange for such compliance directly or as TENANT'S agent through contractors or other parties selected by CITY at TENANT'S expense (without limiting CITY'S other remedies under this Lease or applicable law).

Section 3.06 Tidelands Trust.

TENANT shall use and occupy the Premises in strict compliance with the Tidelands Trust purposes under which the Premises or any portion thereof are held by CITY pursuant to the grants from the State of California as set forth in this Lease.

Section 3.07 Compliance with Law.

TENANT shall, at no cost to CITY, comply with all of the requirements of all local, municipal, county, state and federal authorities now in force, or which may hereafter be in force, pertaining to the Premises, and shall faithfully observe in the use of the Premises all local, municipal and county ordinances and state and federal statutes, rules, regulations and orders now in force or which may hereafter be in force (collectively, "Legal Requirements") provided that TENANT shall not be required to comply with any Legal Requirement imposed by the CITY that would substantially deprive TENANT of a material benefit under this lease unless such Legal Requirement has been imposed or required by a county, state or federal authority. The judgment of any court of competent jurisdiction, or the admission of TENANT in any action or proceeding against TENANT, whether CITY be a party thereto or not, that TENANT has

violated any such Legal Requirement in the use of the Premises shall be conclusive of that fact as between CITY and TENANT.

Section 3.08 Waste or Nuisance.

TENANT shall not commit or permit the commission by others of any waste on the Premises; TENANT shall not maintain, commit, or permit the maintenance or commission of any nuisance as defined by law on the Premises; and TENANT shall not use or permit the use of the Premises for any unlawful purpose.

Section 3.09 Use by CITY.

(1) Subject to TENANT's rights hereunder to possession of the Premises, CITY may grant licenses to, or otherwise authorize, other persons and entities permitting uses of the Morro Bay Harbor.

(2) CITY also retains and reserves for itself, its successors and assigns, all oil, gas, petroleum and other mineral or hydrocarbon substances in and under the lands leased hereby together with right to prospect and extract all such substances.

Article 4 CONSTRUCTION, ALTERATION AND REPAIRS

Section 4.01 Construction Approval.

(1) TENANT shall not make or permit any other person to make any alterations or structural additions or structural modifications to the Premises or to any structure thereon or facility appurtenant thereto if the cost thereof shall exceed ten thousand dollars (\$10,000), without the prior written consent of CITY. The consent to be obtained pursuant to this Section 4.01(1) shall be requested from the Harbor Director, or the City's designee, for CITY. If the Harbor Director or any future successor to the duties of the City's Harbor Director, or the City's designee, gives such consent to proceed, then it is understood such consent is given by CITY only in its capacity as the landlord under this Lease and not as the permit-issuing authority. TENANT remains obligated to obtain any needed building permits and comply with all applicable planning processes.

(2) Where required by the Morro Bay Municipal Code, California Coastal Act, Corps of Engineers or any other state or federal agency having authority over the proposed project, then all Conditional Use Permits, Concept Plans, Precise Plans, Coastal Development Plans, and any other required plans or permits shall be applied for and approved prior to any construction, alteration or repairs.

Section 4.02 Construction Bond.

(1) Prior to the commencement of any construction the cost of which is greater than the amount of one hundred thousand dollars (\$100,000), TENANT shall file with CITY'S City Clerk a final detailed Civil Engineer's, Registered Architect's or Licensed and Bonded General Contractor's estimate of the cost of construction and installation of improvements on the Premises. Said estimate must be submitted to CITY'S City Engineer for approval. TENANT shall file with the City Clerk a faithful performance bond, in a form and issued by a corporate surety company satisfactory to CITY, in an amount satisfactory to CITY but not in excess of one hundred percent (100%) of the final detailed cost estimate, securing the faithful performance of TENANT or its contractor in the completion of said construction.

(2) TENANT shall also file with the Morro Bay CITY Clerk a labor and materials bond, in a form and issued by a corporate surety company satisfactory to CITY, in an amount satisfactory to CITY but not in excess of one hundred percent (100%) of the final detailed cost estimate, securing the payment of all claims for the performance of labor or services on, or the furnishing of materials for, the performance of said construction.

(3) In lieu of the above referenced bonds, TENANT may post cash deposits or may make other mutually satisfactory arrangements to guarantee the completion of construction projects. In the event the contractor bonds the project, CITY may be named as additional indemnitee to comply with these requirements.

Section 4.03 Mechanics' Liens.

At all times during the term of this Lease, TENANT shall keep the Premises and all buildings, installations and other improvements now or hereafter located on the Premises free and clear of all liens and claims of liens for labor, services, materials, supplies, or equipment performed on or furnished to the Premises. TENANT further agrees to at all times, save CITY free and harmless and indemnify CITY against all claims for labor or materials in connection with any improvement, repairs, or alterations on the Premises, and the cost of defending against such claims, including reasonable attorneys' fees. Should TENANT fail to pay and discharge or cause the Premises to be released from such liens or claim of liens within ten (10) days after the filing of such lien or levy, TENANT shall upon written notification be required to immediately deposit with CITY a bond conditioned for payment in full of all claims on which said lien or levy has been filed. Such bond shall be acknowledged by TENANT as principal and by a company or corporation, licensed by the Insurance Commissioner of the State of California to transact the business of a fidelity and surety insurance company as surety. The beneficiary of any security instrument which instrument is on record with CITY, shall have the right to file such a bond on

behalf of TENANT. CITY shall have right to post and keep posted on the Premises notices of non-responsibility and any other notices that may be provided by law or which CITY may deem proper for the protection of CITY and Premises from such liens. TENANT shall give CITY notice at least twenty (20) days prior to commencement of any work on the Premises to afford CITY the opportunity to post such notices.

Section 4.04 Ownership of Improvements.

The parties agree CITY has the option and right to require TENANT to remove all buildings, structures, installations, improvements of any kind or other property belonging to or placed upon the Premises by TENANT at the termination of this Lease, however occurring, providing CITY gives notice, in writing, no later than thirty (30) days prior to the termination of the Lease, of its decision to require that such improvements be removed. The parties agree that if the CITY exercises its option, then at the termination of this Lease, however occurring, TENANT shall have sixty (60) days thereafter to remove all buildings, structures, facilities, installations, improvements and other property belonging to TENANT from the Premises. If CITY exercises such option and TENANT fails to remove all such improvements and other property within sixty (60) days after the termination of this Lease, then CITY shall have the right to have any or all such improvements and other property removed at the expense of TENANT. If CITY does not exercise its option to remove (or require the removal of) the improvements and other property, then title to such improvements and other property shall vest in CITY and TENANT shall not remove same.

Article 5 LEASEHOLD MORTGAGES

Tenant shall not mortgage, securitize or hypothecate the leasehold interest in whole or any part without the prior written approval of CITY as evidenced by a resolution of the City Council of CITY.

Article 6 REPAIRS, MAINTENANCE AND RESTORATION

Section 6.01 Maintenance by TENANT.

At all times during the term of this Lease, TENANT shall, at TENANT'S own cost and expense, keep and maintain all improvements now or hereafter on the Premises in good order and repair and in a safe and clean condition. Furthermore, TENANT shall, at TENANT'S own cost and expense, maintain at all times during the term of this Lease the whole of the Premises in a clean, sanitary, neat and orderly condition. CITY may, at the sole option of CITY, clean and

clear the Premises, at TENANT'S cost and expense, in the event TENANT fails to clean and clear the Premises in accordance with this Section to the satisfaction of CITY after 15-days' written notice to TENANT from CITY of CITY'S intent to exercise this option.

Section 6.02 Seawalls and Revetment.

At all times during the term of this Lease, TENANT shall at TENANT'S own cost and expense repair, maintain, replace and rebuild as necessary, the improvements, pilings, bulkheads, seawalls, revetment, piers, posts and any structures or other improvements located in the water portion of the Premises. Further, TENANT shall at TENANT'S own cost and expense conduct maintenance surveys at reasonable intervals to locate and determine needed repairs.

Section 6.03 Legal Requirements.

At all times during the term of this Lease, TENANT, at no cost to CITY, shall:

- (1) Make all alterations, additions, or repairs to the Premises or the improvements or facilities on the Premises required by any Legal Requirements (as defined in Section 3.07 above) now or hereafter made or issued;
- (2) Observe and comply with all Legal Requirements now or hereafter made or issued respecting the Premises or the improvements or facilities located thereon;
- (3) Obtain all required permits pursuant to the Morro Bay Municipal Code or State law prior to the initiation of any repair or maintenance activity; and
- (4) Indemnify and hold CITY and the property of CITY, including the Premises, free and harmless from any and all liability, loss, damages, fines, penalties, claims and actions resulting from TENANT'S failure to comply with and perform the requirements of this section.

Section 6.04 Failure to Repair.

In the event failure to repair results in a hazardous or unsafe condition, CITY shall have the right and option but not the obligation to close and prohibit access to the unsafe portion of the Premises until such repairs are completed and accomplished and the Premises rendered safe for public use. In addition, if TENANT fails to repair any hazardous or unsafe condition within ten (10) days after written notice thereof from CITY, CITY shall have the right, but not the obligation, to perform such repair at TENANT'S expense. TENANT shall reimburse CITY for any such repair undertaken by CITY, promptly upon CITY'S demand, as additional Rent. Failure by CITY to enforce any of the provisions of this Article shall not constitute a waiver of these provisions and CITY may at any time enforce all of the provisions of this Article, requiring all necessary repairs, rebuilding or replacement.

Section 6.05 Inspection by CITY.

CITY or CITY'S agents, representatives, or employees may enter the Premises at all reasonable times for the purpose of inspecting the Premises to determine whether TENANT is complying with the terms of this Lease and for the purpose of doing other lawful acts that may be necessary to protect CITY'S interest in the Premises under this Lease or to perform CITY'S duties under this Lease.

Section 6.06 TENANT'S Duty to Restore Premises.

(1) Except as provided in Section 6.07 below, if at any time during this Lease, any improvements now or hereafter on the Premises are destroyed in whole or in part by the elements, or any other cause not the fault of TENANT or CITY, this Lease shall continue in full force and effect and TENANT, at TENANT'S own cost and expense, shall repair and restore the damaged or destroyed improvement(s) according to the original plan thereof or according to such modified plans therefore as shall be approved in writing by CITY. The work of permitting, repair and restoration shall be commenced by TENANT within one hundred eighty (180) days after the damage or destruction occurs shall be pursued with due diligence, and shall be completed not later than one year after the work is commenced, unless the parties hereto mutually agree, in writing, to an extension. In all other respects, the work of repair and restoration shall be done in accordance with the requirements for construction work on the Premises set forth in Article 4 of this Lease. Any failure by TENANT either to commence or to complete repair and restoration as required by this Section 6.06 shall be a material default under this Lease.

(2) Any and all insurance proceeds that become payable at any time during the term of this Lease because of damage to or destruction of any improvements on the Premises shall be paid to TENANT and applied by TENANT toward the cost of repairing and restoring the damaged or destroyed improvements in the manner required by this Section 6.06, or, if this Lease is terminated, then applied as provided in Section 6.07. Except as set forth in Section 6.08 below, TENANT'S obligation to restore pursuant to this Section shall exist whether or not funds are available from insurance proceeds.

Section 6.07 Termination of Lease for Destruction.

(1) Notwithstanding the provisions of Section 6.06 of this Lease, TENANT shall have the option of terminating this Lease as provided in this Section 6.07 if:

(a) During the last fifteen (15) years of the term of this Lease, any improvements now or hereafter on the Premises are so damaged or destroyed by the elements or any cause not

the fault of TENANT or CITY they cannot be repaired and restored as required by Section 6.06 of this Lease at a cost not exceeding thirty-five percent (35%) of the cost of replacing all improvements if they had been totally destroyed at the time of such damage; or

(b) During the last ten (10) years of the term of this Lease, any improvements now or hereafter on the Premises are so damaged or destroyed by the elements or any cause not the fault of TENANT or CITY they cannot be repaired and restored as required by Section 6.06 of this Lease at a cost not exceeding fifteen percent (15%) of the cost of replacing all improvements if they had been totally destroyed at the time of such damage.

(2) TENANT may exercise its right to terminate pursuant to this Section 6.07 by providing written notice to CITY within one hundred eighty (180) days following damage or destruction as described herein. Such termination shall be effective on the last day of the calendar month following the month in which TENANT provides its notice.

(3) If TENANT fails to commence or complete repair and restoration as required by Section 6.06, then CITY shall have all rights and remedies with respect to TENANT's default, including but not limited to termination of this Lease pursuant to Article 11.

(4) If this Lease is terminated as a result of damage or destruction, then any insurance proceeds received with respect to the improvements shall be applied or distributed in the following order:

(a) first, to the demolition of the improvements and removal of all demolition debris; then

(b) to any accrued and unpaid Rent as of the effective date of the termination; then

(c) to each Lender under a Leasehold Encumbrance, in order of lien priority, an amount not to exceed the amount due under such Leasehold Encumbrance; then

(d) to CITY, an amount equal to the present value, as of the date of termination, of the total Minimum Rent for the remainder of the Term; then

(e) the remaining proceeds, if any, to TENANT.

Section 6.08 Destruction Due to Risk Not Covered by Insurance.

Notwithstanding anything to the contrary in Section 6.06 of this Lease, TENANT shall have the right to terminate this Lease at any time if the improvements on the Premises are

damaged or destroyed by a casualty not caused by the fault of TENANT or CITY and for which TENANT is not required under this Lease to carry insurance and the cost to repair or restore such improvements exceeds fifty percent (50%) of the fair market value of all the improvements on the Premises immediately prior to the damage or destruction.

Article 7 INDEMNITY AND INSURANCE

Section 7.01 Indemnity Agreement.

(1) TENANT shall indemnify and hold harmless CITY, and the property of CITY (including the Premises and any improvements now or hereafter on the Premises), and the CITY'S officers, officials, employees and volunteers from any and all liability, claims, loss, damages, and expenses, including attorney fees and litigation expenses, resulting from TENANT'S occupation and use of the Premises or any negligent act or omission of the TENANT or any of its subtenants, employees, contractors or anyone for whom TENANT may be liable, specifically including, without limitation, any liability, claim, loss, damage, or expense arising by reason of:

(a) The death or injury of any person, including TENANT or any person who is an employee or agent of TENANT, or by reason of the damage to or destruction of any property, including property owned by TENANT or by any person who is an employee or agent of TENANT, from any cause whatever while such person or property is in or on the Premises or in any way connected with the Premises or with any of the improvements or personal property on the Premises;

(b) The death or injury of any person, including TENANT or any person who is an employee or agent of TENANT, or by reason of the damage to or destruction of any property, including property owned by TENANT or any person who is an employee or agent of TENANT, caused or allegedly caused by either (i) the condition of the Premises or any improvement placed on the Premises by TENANT, or (ii) any act or omission on the Premises by TENANT or any person in, on, or about the Premises with or without the permission and consent of TENANT;

(c) Any work performed on the Premises or materials furnished to the Premises at the instance or request of TENANT or any person or entity acting for or on behalf of TENANT;

(d) TENANT'S failure to perform any provision of this Lease or to comply with any Legal Requirement imposed on TENANT or the Premises.

(2) TENANT'S obligations pursuant to this Section to indemnify and hold harmless do not extend to any liability, claim, loss, damage or expense arising from CITY'S active negligence or willful misconduct.

Section 7.02 Liability Insurance.

During the term of this Lease, TENANT shall maintain at its cost Commercial General Liability insurance with coverages at least as broad as ISO Forms labeled "City of Morro Bay Insurance requirements for Lessees", Certificate of Insurance – City of Morro Bay", and "Additional Insureds – Managers or Lessors of Premises" attached hereto as Exhibit B and made a part hereof as may be updated or changed from time to time at the sole discretion of the CITY, insuring against claims for bodily injury (including death), property damage, contractual liability, personal injury and advertising injury occurring on the Premises or from operations located in any part of the Premises. Such insurance shall afford protection in amounts no less than One Million Dollars (\$1,000,000) per occurrence for bodily injury, personal injury and property damage, provided that if insurance with a general aggregate limit is used, either the general aggregate limit shall apply separately to the Premises or the general aggregate limit shall be twice the occurrence limit stated in this Section. All liability insurance carried by TENANT hereunder shall name CITY, its officers, officials, employees and volunteers as additional insureds, and shall be primary insurance with respect to such additional insureds. TENANT shall include all its subtenants as insureds under TENANT's liability policies or shall furnish separate certificates and endorsements for each subtenant. All coverages for subtenants shall comply with all requirements of this Article Seven.

Section 7.03 Worker's Compensation.

TENANT shall maintain at TENANT'S own expense and keep in full force and effect during the term of this Lease, Worker's Compensation Insurance as provided by law. Said insurance shall contain a waiver of subrogation rights against CITY. TENANT shall also maintain employer's liability insurance with minimum coverage of \$1,000,000 per accident for bodily injury or disease.

Section 7.04 Property Insurance.

TENANT shall, at its cost, at all times during the term of this Lease keep all improvements and other structures on the Premises, as well as any and all additions, improvements and betterments thereto, insured for one hundred percent (100%) of their full replacement cost with no co-insurance provision against loss or destruction by the perils covered by "all risk" (excluding earthquake) property damage insurance policies. Any loss payable under

such insurance shall be payable to TENANT, CITY, and any Lender under a Leasehold Encumbrance pursuant to Article 5 of this Lease, as their interests may appear, and such proceeds shall be used and applied in the manner required by Article 6 of this Lease.

Section 7.05 Additional Coverage.

TENANT shall also maintain, at its expense, the insurance described in this Section 7.05.

(1) If TENANT has (or is required by any Legal Requirement to have) a liquor license and is selling or distributing alcoholic beverages on the Premises, then TENANT shall maintain liquor liability coverage in appropriate amounts. TENANT shall require any subtenant who has (or is required by any Legal Requirement to have) a liquor license and who is selling or distributing alcoholic beverages on the Premises, to maintain such coverage.

(2) TENANT shall maintain "all risk" (excluding earthquake) property damage insurance covering TENANT's personal property located at the Premises, in amounts not less than the full replacement value of such personal property. CITY shall have no interest in the proceeds of such insurance.

(3) TENANT shall, at TENANT's own expense, obtain and maintain any additional insurance coverages that CITY may reasonably require. As illustration only and not as a limitation, in appropriate circumstances such additional insurance may include increased general liability limits, business interruption coverage, business automobile liability, boiler and machinery insurance and/or builder's risk insurance. However, TENANT shall not be required to maintain additional coverages that are in excess of those typically maintained by similarly situated tenants in the Morro Bay area.

Section 7.06 General Requirements.

Except as specifically provided to the contrary, all the insurance required pursuant to this Article 7 shall be subject to the requirements of this Section 7.06.

(1) Maintenance of proper insurance coverage is a material element of this Lease and failure to maintain or renew coverage or to provide evidence of coverage and/or renewal may be treated by the CITY as a material breach of contract. TENANT shall forward the CITY specifications and forms to TENANT'S insurance agent for compliance.

(2) CITY may at any time require TENANT to increase the minimum coverage limits for insurance required by this Lease, but every such increase shall be reasonable under the circumstances.

(3) All policies shall be issued by insurance companies authorized to issue such insurance in California, with an A.M. Best's rating of no less than A:VII.

(4) Any deductibles or self-insured retentions must be declared to and approved by CITY. At the option of CITY, either: the insurer shall reduce or eliminate such deductibles or self-insured retentions as respects CITY, its officers, officials, employees and volunteers; or the TENANT shall provide a financial guarantee satisfactory to CITY guaranteeing payment of losses and related investigations, claim administration and defense expenses.

(5) Each insurance policy required by this Lease shall be endorsed to state that coverage shall not be cancelled or reduced, except after thirty-30-days' prior written notice by certified mail, return receipt requested, has been given to CITY.

(6) TENANT shall furnish CITY with certificates and amendatory endorsements effecting the coverage required by this Lease. The endorsements shall be on forms provided by CITY or on other than CITY's forms, provided those endorsements or policies conform to the requirements. All certificates and endorsements are to be received and approved by CITY before use of the Premises, and promptly following any renewal or replacement. CITY reserves the right at any time to require complete, certified copies of all required insurance policies, including endorsements effecting the coverage required by these specifications.

(7) TENANT's insurance coverage shall be primary insurance as respects CITY, its officers, officials, employees, and volunteers. Any insurance or self-insurance maintained by CITY, its officers, officials, employees, or volunteers shall be excess of TENANT's insurance and shall not contribute with it.

Section 7.07 No Subrogation.

TENANT agrees that in the event of loss due to any of the perils for which it has agreed to provide insurance, TENANT shall look solely to its insurance for recovery. TENANT hereby grants to the CITY, on behalf of any insurer providing insurance to either TENANT or CITY with respect to TENANT'S occupancy of the Premises, a waiver of any rights to subrogation which any such insurer of said TENANT may acquire against the CITY by virtue of the payment of any loss under such insurance. Each insurance policy required under this Lease including those insuring TENANT against claims, expense, or liability for injury to persons or property shall provide that the insurer shall not acquire by subrogation any right to recovery which TENANT has expressly waived in writing prior to the occurrence of the loss.

Section 7.08 TENANT'S Waiver.

TENANT hereby waives any right of recovery against CITY for each claim, expense, liability, or business interruption, or other loss, except where caused by CITY'S active negligence or willful misconduct. TENANT agrees that to the extent that TENANT fails to acquire insurance, TENANT shall not have any claim against CITY for any loss that results from a risk or peril that would have been included in such insurance.

Section 7.09 Insurance Not a Limit.

The insurance requirements of this Article Seven are independent of, and do not limit or modify, TENANT'S indemnification and other obligations pursuant to this Lease.

Article 8 TAXES AND FEES

Section 8.01 TENANT to Pay Taxes.

TENANT shall pay, before delinquency, all taxes and assessments levied upon or assessed to TENANT on the Premises by reason of this Lease or of any equipment, appliances, improvement, or other development of any nature whatsoever, erected, installed, or maintained by TENANT or by reason of the business or other activity of TENANT upon or in connection with the Premises. TENANT shall pay all possessory interest taxes applicable to the Premises.

Section 8.02 TENANT to Pay License and Permit Fees.

TENANT shall pay any fees imposed by law for licenses or permits for any business or activities including construction by TENANT upon the Premises.

Section 8.03 Utilities.

TENANT shall pay, or cause to be paid, and hold CITY and the property of CITY, including the Premises, free and harmless from all charges for the furnishing of gas, water, electricity, telephone service, and for other public utilities to the Premises during the term of this Lease and for the removal of garbage and rubbish from the Premises during the term of this Lease.

Article 9 CONDEMNATION

Section 9.01 Total Condemnation.

If title and possession to all of the Premises is permanently taken for any public or quasi-public use under any statute, or by the right of eminent domain, then this Lease shall terminate on the date that possession of the Premises is taken, and both CITY and TENANT shall thereafter be released from all obligations, including Rent, all of which shall be prorated to the date of termination, except those specified in Section 9.02 of this Lease.

Section 9.02 Condemnation Award.

Any compensation or damages awarded or payable because of the permanent taking of all or any portion of the Premises by eminent domain shall be allocated between CITY and TENANT as follows:

(1) All compensation or damages awarded or payable for the taking by eminent domain of any land that is part of the Premises shall be paid to and be the sole property of CITY free and clear of any claim of TENANT or any person claiming rights to the Premises through or under TENANT.

(2) All compensation or damages awarded or payable which is specifically attributed by the taking party to the "good will" of TENANT'S business shall be paid to and be the sole property of TENANT.

(3) All compensation or damages awarded or payable because of any improvements constructed or located on the portion of the Premises taken by eminent domain where only a portion of the Premises is taken by eminent domain, and TENANT is not entitled to or does not terminate this Lease, shall be applied in the manner specified in Section 9.04 toward the replacement of such improvements with equivalent new improvements on the remaining portions of the Premises.

(4) All compensation or damages awarded or payable because of any improvements constructed or located on the portion of the Premises taken by eminent domain where this Lease is terminated because of the taking by eminent domain, whether all or only a portion of the Premises is taken by eminent domain, shall be allocated between CITY and TENANT as follows:

(a) That percentage of the compensation or damages awarded or payable because of the improvements that equals the percentage of the full term of this Lease that has, at the time of the taking, not expired shall belong to and be the sole property of TENANT.

(b) That percentage of the compensation or damages awarded or payable because of the improvements that equals the percentage of the full term of this Lease that has, at the time of the taking, expired shall belong to and be the sole property of CITY.

(c) The term "time of taking" as used in this Section shall mean 12:01 a.m. of the date that the agency or entity exercising the eminent domain power, takes, title, or the date that it takes physical possession of the portion of the Premises, whichever shall first occur.

(5) Any severance damages awarded or payable because only a portion of the Premises is taken by eminent domain shall be the sole and separate property of CITY.

Section 9.03 Termination for Partial Taking.

If, during the term of this Lease, title and possession of only a portion of the Premises is taken for any public or quasi-public use under any statute, or by right of eminent domain, then TENANT may, at TENANT'S option, terminate this Lease by serving written notice of termination on CITY within ninety (90) days after TENANT has been deprived of actual physical possession of the portion of the Premises taken for such public use. This Lease shall terminate on the first day of the calendar month following the calendar month in which the notice of termination described in this section is served on CITY. On termination of this Lease pursuant to this Article, all subleases and subtenancies in or on the Premises or any portion of the Premises created by TENANT under this Lease shall also terminate and the Premises shall be delivered to CITY free and clear of all such subleases and subtenancies; provided, however, that CITY may, at CITY'S option, by mailing written notice to a subtenant allow any subtenant to attorn to CITY and continue such subtenant's occupancy on the Premises as a TENANT of CITY. On termination of this Lease pursuant to this section, however, both CITY and TENANT shall be released from all obligations under this Lease, except those specified in Section 9.02 of this Lease.

Section 9.04 Rent Abatement for Partial Taking.

If, during the term of this Lease, title and possession of only a portion of the Premises is taken under the power of eminent domain by any public or quasi-public agency or entity and TENANT does not terminate this Lease, then this Lease shall terminate as to the portion of the Premises taken under eminent domain on the date actual physical possession of the portion taken by eminent domain is taken by the agency or entity exercising the eminent domain power. Furthermore, the Rent payable under this Lease shall, as of that time be reduced in the same proportion of the Premises taken by eminent domain bears to the full value of the Premises at that time; provided however, that TENANT shall make a good faith effort to replace any

improvements or facilities with equivalent new facilities on the remaining portion of the Premises and do all other acts at TENANT'S own cost and expense required by the eminent domain taking to make the remaining portion of the Premises fit for the use specified in this Lease.

Section 9.05 Conveyance in Lieu of Eminent Domain.

A voluntary conveyance by CITY, with the consent of TENANT, of title to all or a portion of the Premises to a public or quasi-public agency or entity in lieu of and under threat by such agency or entity to take the same by eminent domain proceedings shall be considered a taking of title to all or such portion of the Premises under the power of eminent domain subject to the provisions of this Article.

Section 9.06 Temporary Taking.

If the possession of the Premises or any portion thereof is taken under the power of eminent domain by any public or quasi-public agency or entity for a limited period not extending beyond the term of this Lease, then this Lease shall not terminate (except as provided in this Section 9.06) and TENANT shall continue to perform all its obligations hereunder, except only to the extent that TENANT is prevented from performing such obligations by reason of such taking. TENANT shall be entitled to receive the entire amount of compensation or damages awarded because of such temporary taking. If a temporary taking extends for more than thirty-six (36) months, then TENANT shall have the right to terminate this Lease, and TENANT shall be entitled to receive, out of the compensation or damages awarded because of such temporary taking, the amount that is attributable to the period of time up until the effective date of TENANT'S termination of this Lease.

Article 10 ASSIGNMENT AND SUBLEASING

Section 10.01 No Assignment Without CITY'S Consent.

Except as provided in this Article 10, TENANT shall not assign or otherwise transfer this Lease, any right or interest in this Lease, or any right or interest in the Premises or any of the improvements that may now or hereafter be constructed or installed on the Premises without the express written consent of CITY evidenced by resolution first had and obtained. Any assignment or transfer by TENANT without the prior written consent of CITY, whether it be voluntary or involuntary, by operation of law or otherwise, is void and shall, at the option of CITY, terminate this Lease. A consent by CITY to one assignment shall not be deemed to be a

consent to any subsequent assignment of this Lease by TENANT. CITY shall not unreasonably nor arbitrarily withhold its approval to the assignment or transfer of this Lease to an assignee who is financially reliable and qualified to conduct the business for which this Lease was granted. It is mutually agreed that the TENANT'S qualifications are a part of the consideration for granting of this Lease and said party does hereby agree to maintain active control and supervision of the operation conducted on the Premises.

Section 10.02 Change of Ownership as Assignment.

For purposes of this Article 10, the following transactions will be deemed to be assignments or transfers:

(1) If TENANT is a partnership or limited liability company:

(a) A change in ownership effected voluntarily, involuntarily, or by operation of law, within a twelve-month (12-month) period, of twenty-five percent (25%) or more of the partners or members or twenty-five percent (25%) or more of the partnership or membership interests; or

(b) The dissolution of the partnership or limited liability company without its immediate reconstitution.

(2) If TENANT is a corporation whose stock is not publicly held and not traded through an exchange or over the counter:

(a) The sale or other transfer, within a twelve-month (12-month) period, of more than an aggregate of twenty-five percent (25%) of the voting shares of TENANT (other than to immediate family members by reason of gift or death); or

(b) The dissolution, merger, consolidation, or other reorganization of TENANT.

Section 10.03 Application for Assignment.

A condition of an assignment shall be TENANT shall file with the CITY an application to assign the leasehold prepared by the prospective assignee. Concurrently with filing the application, TENANT shall pay a reasonable fee associated with the cost of processing said application, in cash or certified or cashier's check to enable CITY adequately to investigate the proposed assignee's qualifications as a permitted assignee. CITY shall not be required to account for the use of the sum paid. If the proposed assignee's net worth on the date of assignment is not sufficient to reasonably guarantee successful operation of the Premises in compliance with all applicable CITY, County, State and federal requirements, then CITY may withhold approval of

the assignment or condition it upon TENANT'S guarantee of such assignee's obligations hereunder for such period as CITY deems advisable. Net worth shall mean the amount by which the total of all assets shall exceed the total of all liabilities as determined in accordance with general accepted accounting principles as approved by CITY'S auditor, or other authorized representative or agent.

Section 10.04 Probate Transfer of Assignment.

If TENANT is an individual, then nothing herein contained will prevent the transfer of this Lease by will, or by operation of law under the intestacy provisions of the California Probate Code as it may be amended from time to time. Probate sale of the leasehold interest will not be permitted without the consent of CITY, evidenced by resolution, first had and obtained.

Section 10.05 No Sublease Without CITY'S Consent.

TENANT shall not sublease the whole nor any part of the Premises, or license, permit, or otherwise allow any other person (the employees of TENANT excepted) to occupy or use the Premises, or any portion thereof, without the prior written consent of CITY's Harbor Director, or any future successor to the duties of the City's Harbor Director. A consent to one subletting, occupation, licensing or use shall not be deemed to be a consent to any subsequent subletting, occupation, licensing or use by another person. Any sublease or license without CITY'S written consent shall be void, and shall at CITY'S option, terminate this Lease. CITY shall not unreasonably nor arbitrarily withhold its consent to sublet to one who is qualified and financially reliable. CITY'S consent to any occupation, use, or licensing shall be in CITY'S sole and absolute discretion. Notwithstanding any provisions herein to the contrary, the terms "assignment," "subletting," "occupation," or "use," shall not be construed or interpreted to mean or include the temporary, short term renting or leasing of boat slips, motel, hotel, or apartment accommodations on the premises.

Section 10.06 Subtenant Subject to Lease Terms.

Any and all subleases shall be expressly made subject to all the terms, covenants, and conditions of this Lease. In no event shall the term of any sublease extend beyond the term of this Lease. Subject to Section 10.09, termination of this Lease prior to the expiration of this Lease term shall also terminate any and all subleases. A breach of the terms of this Lease by a subtenant shall constitute a breach on the part of TENANT and shall subject both the subtenant and TENANT to all the remedies provided to CITY herein and by law. Failure by any subtenant to report Gross Sales or to pay Percentage Rent due from subtenant shall constitute a breach of

this lease. TENANT hereby agrees to and does guarantee payment of such Percentage Rent due by a subtenant under the terms of this lease.

Section 10.07 Consent Form Agreement.

Prior to any consent by CITY to any sublease hereof, TENANT shall cause to be executed between TENANT and any subtenant an agreement making the CITY a third party beneficiary, in a form acceptable to CITY, whereby the subtenant agrees to be bound by all of the terms, covenants and conditions of this Lease. Further, it is agreed by TENANT that any default by the subtenant of any of the terms, covenants and conditions of this Lease shall be deemed to be violations by TENANT of this Lease and that all remedies of CITY for such violation, including termination of this Lease, shall immediately be enforceable by CITY against TENANT. TENANT shall apply any and all monies received from any subtenant first to the payment of obligations of the subtenant to CITY.

Section 10.08 TENANT and Guarantor Remain Liable.

Prior to approval by CITY to any sublease hereof, TENANT shall agree to be primarily and jointly and severally liable to CITY for all obligations due CITY by any subtenant, including the payment of rents, and TENANT shall agree that CITY may proceed directly against TENANT for any obligation owing CITY by the subtenant. If this Lease is guaranteed, neither the sublease nor CITY'S approval thereof shall release the guarantor from its obligations pursuant to the guaranty.

Section 10.09 Nondisturbance.

On the terms set forth below, CITY may enter into agreements with subtenants; provided, that in the event of any termination of this Lease prior to the expiration date, CITY will not terminate or otherwise disturb the rights of the subtenant under such sublease, but will instead honor such sublease as if such agreement had been entered into directly between Landlord and such subtenant, conditioned upon such subtenant's agreement to attorn to Landlord and full performance of all obligations under the sublease in question ("Non-Disturbance Agreement"). CITY agrees to execute a Non-Disturbance Agreement in connection with a particular sublease provided that Tenant provides CITY with a copy of the sublease, and the Non-Disturbance Agreement is customary in form and substance and otherwise reasonably acceptable to CITY.

Article 11 DEFAULT AND TERMINATION

Section 11.01 Abandonment by TENANT.

If TENANT breaches this Lease and abandons all or any part of the Premises prior to the scheduled expiration of the term of this Lease, then CITY may continue this Lease in effect by not terminating TENANT'S right to possession of the Premises, in which event CITY shall be entitled to enforce all CITY'S rights and remedies under this Lease including the right to recover the Rent specified in this Lease as it becomes due under this Lease.

Section 11.02 Termination for Breach by TENANT.

All covenants and agreements contained in this Lease are declared to be conditions to this Lease and to the term hereby demised to TENANT. If TENANT fails to perform any covenant, condition, or agreement contained in this Lease, except for payment of any Rent or other monetary amount due, and such failure is not cured within thirty (30) days after written notice thereof is served on TENANT, then CITY may terminate this Lease immediately, and in the event of such termination, TENANT shall have no further rights hereunder and TENANT shall thereupon forthwith remove from the Premises and shall have no further right or claim thereto and CITY shall immediately thereupon have the right to re-enter and take possession of the Premises, subject only to appropriate legal process.

Section 11.03 Termination for Failure to Pay Rent.

If any payment of Rent is not made as herein provided and such failure to pay is not cured within three (3) days after written notice thereof is served on the TENANT, then CITY shall have the option to immediately terminate this Lease; and in the event of such termination, TENANT shall have no further right or claim thereto and CITY shall immediately thereupon have the right to re-enter and take possession of the Premises, subject only to appropriate legal process.

Section 11.04 Lender May Cure Default.

CITY shall afford the Lender under any Leasehold Encumbrance of record with CITY the right to cure any default by TENANT of the covenants, conditions, or agreements hereof, as provided in Article 5 of this Lease.

Section 11.05 Attorneys' Fees.

In the event the CITY finds it necessary to retain an attorney in connection with the default by the TENANT or enforcement of any of the terms, conditions, and covenants of this Lease, even though litigation is not instituted, TENANT shall pay to CITY its reasonable attorneys' fees. Non-payment of reasonable attorneys' fees by TENANT within three (3) days after written notice is served on TENANT shall give rise to an independent legal action by CITY to collect same. If CITY is successful in such legal action, then CITY shall also be entitled to reasonable attorney's fees and costs for the collection action.

Section 11.06 Damages for Breach.

If TENANT defaults in the performance of any covenant, condition or agreement contained in this Lease and the default be incurable or not be cured within the time period set forth hereinabove, then CITY may terminate this Lease and:

(1) Bring an action to recover from TENANT:

(a) The worth at the time of award of the unpaid rent which had been earned at the time of termination of the Lease;

(b) The worth at the time of award of the amount by which the unpaid rent which would have been earned after termination of the Lease until the time of award exceeds the amount of rental loss that TENANT proves could have been reasonably avoided;

(c) The worth at the time of award of the amount by which the unpaid rent for the balance of the term after the time of award exceeds the amount of rental loss that TENANT proves could be reasonably avoided; and

(d) Any other amount necessary to compensate CITY for all detriment proximately caused by TENANT'S failure to perform its obligations under this Lease; and

(2) Bring an action, in addition to or in lieu of the action described in subparagraph (1) of this Section, to re-enter and regain possession of the Premises in the manner provided by the laws of unlawful detainer of the State of California then in effect.

Section 11.07 Cumulative Remedies.

The remedies available to CITY in this Article shall not be exclusive but shall be cumulative with and in addition to all remedies now or hereafter allowed by law or elsewhere provided in this Lease.

Section 11.08 Waiver of Breach.

The waiver by CITY of any breach by TENANT of any of the provisions of this Lease shall not constitute a continuing waiver or a waiver of any subsequent breach by TENANT either of the same or a different provision of this Lease.

Section 11.09 Surrender of Premises.

On expiration or sooner termination of this Lease, TENANT shall surrender the Premises, and, subject to Section 4.04, all improvements in or on the Premises, and all facilities in any way appertaining to the Premises, to CITY in good, safe, and clean condition, reasonable wear and tear excepted.

Article 12 MISCELLANEOUS

Section 12.01 Notices.

Any and all notice or demands by or from CITY to TENANT, or TENANT to CITY, shall be in writing. They shall be served either personally, or by registered or certified mail. Any notice or demand to CITY may be given to:

Harbor Director
City of Morro Bay
1275 Embarcadero
Morro Bay, California 93442

with a copy to:

City Manager
City of Morro Bay
595 Harbor Street
Morro Bay, CA 93442

Any notice or demand to TENANT may be given at:

TLC Family Enterprises, Inc.
665 Kings Avenue
Morro Bay, CA 93442

Such addresses may be changed by written notice by either party to the other party.

Section 12.02 Governing Law and Jurisdiction.

This Lease, and all matters relating to this Lease, shall be governed by the laws of the State of California in force at the time any need for interpretation of this Lease or any decision concerning this Lease arises. CITY and TENANT consent to exclusive personal and subject matter jurisdiction in the Superior Court of the State of California in and for the county where the Premises are located, and each party waives any claim that such court is not a convenient forum. Each party hereby specifically waives the provisions of California Code of Civil Procedure Section 394, and any successor statute thereto.

Section 12.03 Binding on Successors.

Subject to the provisions herein relating to assignment and subletting each and all of the terms, conditions, and agreements herein contained shall be binding upon and inure to the benefit of the successors and assigns of any and all of the parties hereto; and all of the parties hereto shall be jointly and severally liable hereunder.

Section 12.04 Partial Invalidity.

If any provision of this Lease is held by a court of competent jurisdiction to be either invalid, void, or unenforceable, then the remaining provisions of this Lease shall remain in full force and effect unimpaired by the holding.

Section 12.05 Sole and Only Agreement.

Subject to the provisions of the second paragraph of Section 1.04, (i) this Lease, including all exhibits incorporated by reference, constitutes the sole and only agreement between CITY and TENANT respecting the Premises and the leasing of the Premises to TENANT and (ii) any other agreements or representations respecting the Premises and their leasing to TENANT by CITY, which are not expressly set forth in this Lease, are null and void. The terms and conditions herein specified correctly set forth the obligations of CITY and TENANT as of the date of this Lease. No modification, amendment, or alteration of this Lease shall be valid unless it is in writing and signed by both parties.

Section 12.06 Modification.

This Lease shall not be modified except pursuant to a written agreement executed by the MAYOR and CITY CLERK pursuant to prior City Council approval. Notwithstanding City Council approval, no agreement shall become effective until such agreement is in fact executed by the MAYOR and CITY CLERK. TENANT understands this Lease may not be modified by

oral statements by any person representing the CITY including the MAYOR and CITY CLERK. TENANT specifically agrees not to rely on oral statements, purported oral waivers, or purported oral modifications and agrees not to rely upon purported written modifications unless they meet the requirements of this paragraph and are approved in writing pursuant to formal City Council action and a subsequent written modification signed by the MAYOR and CITY CLERK. If the title of any person authorized to act for CITY under this Lease shall be changed during the term of this Lease, then the person who succeeds to substantially the same responsibilities with respect to CITY shall have the authority to act for CITY under this Lease.

Section 12.07 Time of Essence.

Time is expressly declared to be the essence of this Lease.

Section 12.08 Memorandum of Lease for Recording.

CITY and TENANT shall, at the request of either at any time during the term of this Lease, execute a memorandum or "short form" of this Lease, which shall describe the parties, set forth a description of the leased premises, specify the term of this Lease, and incorporate this Lease by reference.

Article 13 SPECIAL PROVISIONS PECULIAR TO THIS LEASE SITE

The following provisions apply to this Lease site only:

Section 13.01 Public Restrooms

At least one restroom completed per CUP No. UP0-509 shall be made available to the public during business hours and TENANT shall maintain signage in prominent locations, which clearly identifies the restroom is available to the general public. In the case of a dispute over location and design of signage, the Harbor Director may designate two locations for "public restroom" signs of a type and design to be determined by the CITY. Furthermore, said restroom shall be made available after business hours to slipholders on TENANT'S Lease Site.

Section 13.02 TENANT'S Obligation to Redevelop Site

CITY and TENANT agree TENANT will construct improvements to the Premises as outlined in Conditional Use Permit No. UP0-509 (CUP) consisting of complete demolition of existing improvements and new mixed-use retail, restaurant/bar, convenience food, transient occupancy (hotel) and slips/docks, and including improved vertical and lateral (Harborwalk) public access and outdoor children's play area (Project) and valued at a minimum of \$3,600,000.

Failure to complete the Project and to comply with all conditions of the CUP, as evidenced by a final building permit inspection as required by CITY in its governmental capacity, in addition to providing proof of expenses as evidenced by copies of invoices by the proscribed timeline shall be a material default of the Lease Agreement and subject to any remedies outlined in Article 11 herein, including termination of the Lease.

TENANT acknowledges construction of the Project on the premises as outlined in the CUP requires, but may not be limited to, obtaining a permit from the California Coastal Commission, a City Precise Plan, and a City Building Permit. It is TENANT'S obligation to fully investigate the issues and costs in obtaining those approvals. Failure to obtain any and all required permits and approvals for the Project shall not be a reason for failure to comply with this section. TENANT further acknowledges the CUP and construction of the Project may require repair or replacement of all of portions of the docks, existing buildings, revetments, access ways, sidewalks, drainage systems and other current improvements on the Premises to the standards of the City Engineer and TENANT agrees to meet those standards through review and revision of the final Building Plans prior to issuance of a Building Permit for the construction of improvements on the Premises.

TENANT further agrees to:

- A. In addition to complying with the bonding requirements set forth in Section 4.02, provide evidence of conditional or other financing necessary for completion of the Project, as-approved by the Harbor Director, Finance Director and City Attorney, no later than August 1, 2019.
- B. File a complete application for a Coastal Development permit from the California Coastal Commission for the Project no later than January 8, 2019.
- C. Obtain a Coastal Development Permit and other necessary permits for the Project no later than June 8, 2019.
- D. File a complete application for Precise Plan review by the Planning Commission for the Project no later than September 8, 2019.
- E. Obtain Precise Plan approval from the Planning Commission for the Project no later than January 8, 2020.
- F. File a complete application for construction drawings and plans to obtain a Building Permit for the Project no later than April 7, 2020.

G. Obtain Building Permits for the Project no later than July 9, 2020.

H. Commence construction of the Project no later than December 9, 2020. Commencement shall mean when the TENANT has incurred at least \$50,000 of hard construction costs for actual work satisfactorily completed for the Project on the site pursuant to the approved Building Permit.

I. Completion construction of all components of the Project no later than December 9, 2021. Completion shall mean when the Project is entitled to be issued a final Certificate of Occupancy.

During construction of the Project, TENANT shall take all measures to:

A. Avoid any pollution of the atmosphere or littering of land or water by or originating in or about the Premises or caused by TENANT'S construction activities.

B. Keep the noise level on the Premises to a minimum so that persons in the neighborhood will be able to comfortably enjoy business and facilities in the area.

C. Prevent any pollutants, including but not limited to petroleum products, from entering Morro Bay waters.

D. Avoid negative impacts on surrounding businesses.

E. Prohibit storage of materials or equipment on public property and avoid parking or traffic delays or impairment without prior consent of CITY.

F. Keep the construction site in a slightly, orderly, and safe manner at all times.

Section 13.04 Valet Parking Rent Credit and Hotel Parking Spaces

A. Rent Credit for Valet Services. CITY agrees to credit up to \$25,000, annually, against Rent otherwise due to assist TENANT with paying for parking valet services for Parking Patrons' vehicles to be parked in the Parking Spaces (Rent Credit). The Rent Credit shall be reduced by any revenues received by TENANT for valet parking fees or charges to hotel customers. TENANT shall, on a regular basis, as reasonably requested by CITY'S Harbor Director, provide reports, financial data and other information for CITY'S Financial Director to determine the total amount of Rent Credit to be allowed for that current year. CITY'S City Council shall also annually review this provision. That review will be to determine if changes are warranted and required. If after consultation with TENANT, CITY determines changes are

required and TENANT does not agree with those changes, then CITY may impose the changes, including rescission of some of all of the rent credit, upon 120-days' written notice to TENANT. Unless extended by an amendment to this Lease, the provisions of this Paragraph A. shall terminate on the fifth full calendar year after the issuance of a final Certificate of Occupancy for the Project.

B. Parking Spaces. CITY shall reserve eight spaces at CITY'S parking lot located at the northeast corner of Pacific Street and Market Avenue (Parking Spaces) exclusively for overnight parking of vehicles of patrons staying at the hotel on the Premises (Parking Patrons) during the hours of 3:00 p.m. and 11:00 a.m. TENANT shall pay CITY \$3,400.00 (\$426.25 each) per year for that exclusive use of the Parking Spaces. The Parking Spaces shall be designated by signs (and standards/poles to attach the signs), all provided by TENANT, at its costs, indicating the Parking Spaces are so reserved for Parking Patrons. The signage and standards shall be approved by CITY'S Community Development Director and installed by CITY employees at no additional cost to TENANT. Annually, CITY'S City Council shall review this provision and determine if changes are required to best serve the general public and TENANT. If after consultation with TENANT, CITY determines changes are warranted and required and TENANT does not agree with those changes, then CITY may impose the changes, including rescission of permission to use the Parking Spaces, upon 120-days' written notice to TENANT.

EXECUTED on _____, 20____, at _____ County, California.

CITY OF MORRO BAY

TLC Family Enterprises
a California Corporation

Jamie L. Irons, MAYOR

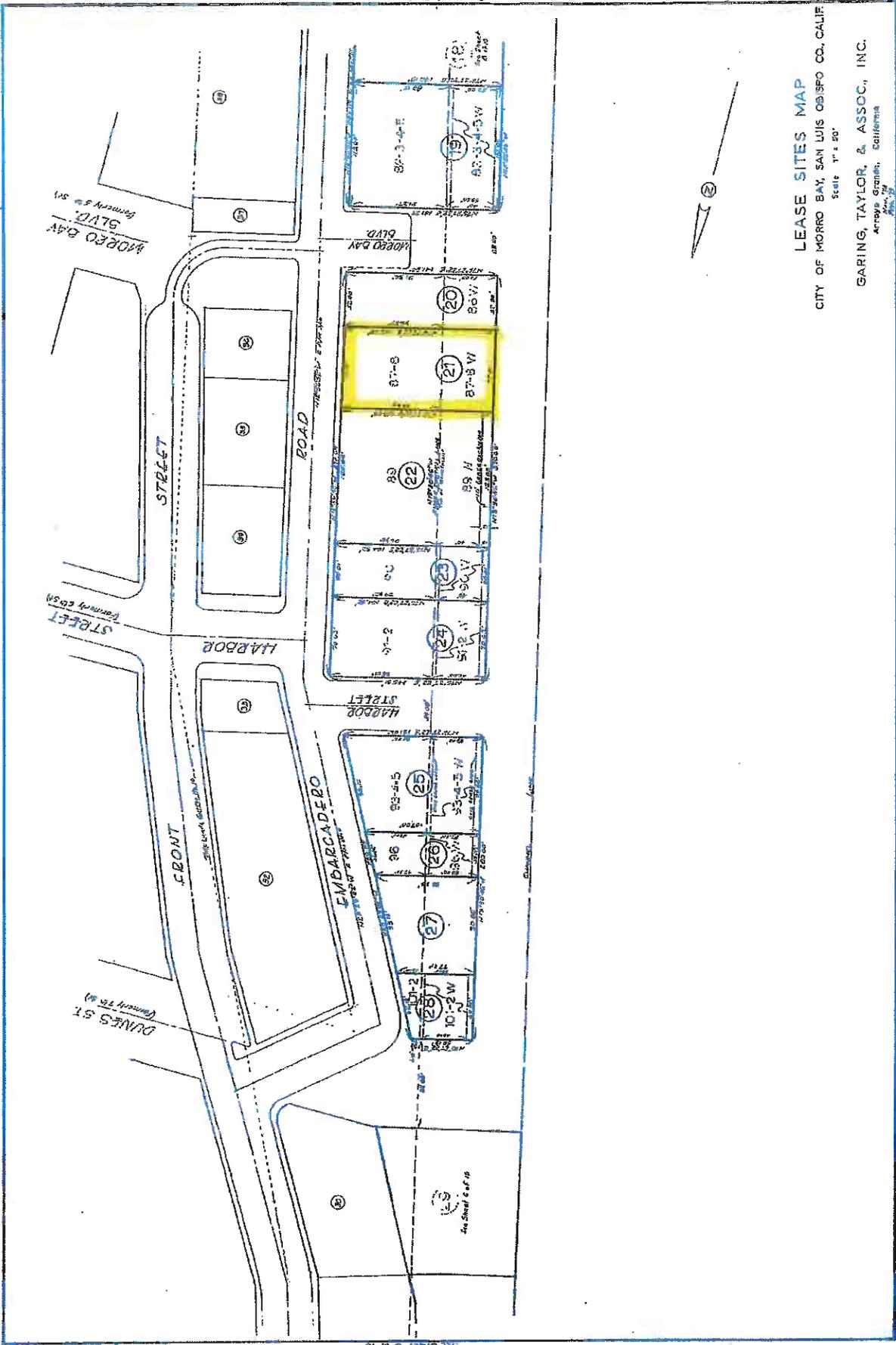
By: _____
it's _____

By: _____
it's _____

ATTEST:

Dana Swanson, CITY CLERK

EXHIBIT A
COPY OF PARCEL MAP



LEASE SITES MAP

CITY OF MORRO BAY, SAN LUIS OBISPO CO., CALIF.
 Scale 1" = 50'

GARING, TAYLOR, & ASSOC., INC.
 Arcata, Calif.
 12/17/79

Sheet 7 of 13



EXHIBIT B

CITY OF MORRO BAY

595 Harbor St.
Morro Bay, CA 93442
(805) 772-6200
FAX (805) 772-7329

INSURANCE REQUIREMENTS FOR LESSEES (NO AUTO RISKS)

Lessee shall procure and maintain for the duration of the contract insurance against claims for injuries to persons or damages to property which may arise from or in connection with the Lessee's operation and use of the leased premises. The cost of such insurance shall be borne by the Lessee.

Minimum Scope of Insurance

Coverage shall be at least as broad as:

1. Insurance Services Office Commercial General Liability coverage (occurrence form CG 0001).
2. Workers' Compensation insurance as required by the State of California and Employer's Liability Insurance (for lessees with employees).
3. Property insurance against all risks of loss to any tenant improvements or betterments.

Minimum Limits of Insurance

Lessee shall maintain limits no less than:

1. General Liability: **\$1,000,000** per occurrence for bodily injury, personal injury and property damage. If Commercial General Liability Insurance or other form with a general aggregate limit is used, either the general aggregate limit shall apply separately to this project/location or the general aggregate limit shall be twice the required occurrence limit.
2. Employer's Liability: **\$1,000,000** per accident for bodily injury or disease.
3. Property Insurance: Full replacement cost with no coinsurance penalty provision.

City of Morro Bay
Insurance Requirements for Lessees

Deductibles and Self-Insured Retentions

Any deductibles or self-insured retentions must be declared to and approved by the City. At the option of the City, either: the insurer shall reduce or eliminate such deductibles or self-insured retentions as respects the City, its officers, officials, employees and volunteers; or the Lessee shall provide a financial guarantee satisfactory to the City guaranteeing payment of losses and related investigations, claim administration and defense expenses.

Other Insurance Provisions

The general liability policy is to contain, or be endorsed to contain, the following provisions:

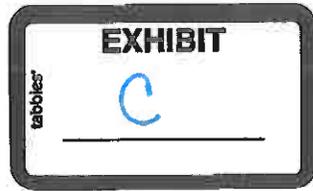
1. The City, its officers, officials, employees, and volunteers are to be covered as insureds with respect to liability arising out of ownership, maintenance or use of that part of the premises leased to the Lessee.
2. The Lessee's insurance coverage shall be primary insurance as respects the City, its officers, officials, employees, and volunteers. Any insurance or self-insurance maintained by the City, its officers, officials, employees, or volunteers shall be excess of the Lessee's insurance and shall not contribute with it.
3. Each insurance policy required by this clause shall be endorsed to state that coverage shall not be canceled, except after 30-days' prior written notice by certified mail, return receipt requested, has been given to the City.

Acceptability of Insurers

Insurance is to be placed with insurers with a current A.M. Best's rating of no less than A:VII.

Verification of Coverage

Lessee shall furnish the City with original certificates and amendatory **endorsements** effecting coverage required by this clause. The endorsements should be on forms provided by the City or on other than the City's forms, provided those endorsements or policies conform to the requirements. All certificates and endorsements are to be received and approved by the City **before** use of City premises. The City reserves the right to require complete, certified copies of all required insurance policies, including endorsements effecting the coverage required by these specifications at any time.



L E A S E

by and between

the CITY OF MORRO BAY

("CITY")

and

TLC FAMILY ENTERPRISES

("TENANT")

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L E A S E

This INTERIM LEASE ("this Lease") is made and entered into by and between the CITY OF MORRO BAY, a municipal corporation of the State of California herein called CITY and TLC Family Enterprises, Inc., a California corporation, herein called TENANT (CITY and TENANT are sometimes collectively referred to as the Parties and individually as the Party.).

WITNESSETH

WHEREAS, the State of California granted certain tide and submerged lands located within the CITY limits of CITY to the County of San Luis Obispo and to its successors, being Chapter 1076, Statutes of 1947, as amended by Chapter 413, Statutes of 1955, Chapter 1874, Statutes of 1957, and Chapter 70, Statutes of 1960, first extraordinary session; which Statutes may be amended from time to time by the Legislature of the State of California; all of which Statutes are expressly recognized and agreed to be in full force and effect by the Parties; and

WHEREAS, the Parties hereto recognize and agree that on July 17, 1964, the CITY of Morro Bay, Lessor herein, succeeded to all of the right, title and interest of the County of San Luis Obispo in and to all of the tide and submerged lands conveyed to said County by the State of California pursuant to the above-mentioned acts; and

WHEREAS, judgment has been entered on October 14, 1968, in the case of CITY of Morro Bay, Plaintiff, versus County of San Luis Obispo, and State of California, Defendants, by the Superior Court of the State of California in and for the County of San Luis Obispo, #30417, adjudging and decreeing, among other things, that the title to said tide and submerged lands so conveyed by the State of California to the County of San Luis Obispo in trust, as set forth above, passed automatically to the CITY of Morro Bay upon the date of its incorporation as a CITY on the 17th day of July, 1964; and

WHEREAS, TENANT accepts the within Lease with full knowledge there is no warranty of title in and to the within described premises by CITY to TENANT; and

WHEREAS, in order to develop and improve Morro Bay Harbor and to assist in carrying out the provisions of the tideland grant as aforesaid, and in order to provide facilities for the accommodation of those using Morro Bay Harbor, CITY desires to lease to TENANT the within described property upon the terms and conditions set forth herein; and

WHEREAS, if this Lease is not otherwise terminated, then the Parties intend to work to negotiate to replace this Lease with another lease, if all the requirements of that certain Consent of Owner, dated February 28, 2018, and signed by the Parties (COL) are timely met.

NOW, THEREFORE, in consideration of the covenants to be performed and the rental to be paid by TENANT to CITY, CITY leases to TENANT, and TENANT leases from CITY, all of the following premises (herein collectively referred to as the Premises) in the CITY of Morro Bay, County of San Luis Obispo, State of California, described as follows: Lease Sites 87-88/87W-88.

This property is delineated on Parcel Map of the CITY of Morro Bay No. 68-30, which map was recorded on October 10, 1968, in Book 3, Page 10 of Parcel Maps in the Office of the County Recorder, San Luis Obispo County, California. A copy of said Map is attached hereto as Exhibit A and made a part hereof by reference.

Article 1 FIXED TERM

Section 1.01 Term.

The term of this Lease shall be deemed to be a period commencing as of April 1, 2018 (the "Commencement Date") and shall terminate, without notice, on October 26, 2018, unless sooner terminated, as herein provided or extended by mutual agreement of the Parties. Notwithstanding the foregoing, the Parties agree, if this Lease is terminated for any reason, and (i) if TENANT is in good standing regarding the terms of this Lease, then CITY and TENANT shall negotiate in good faith a new lease solely for TENANT to continue to operate Under the Sea Gallery in the downstairs portion of the Premises currently occupied by Under the Sea Gallery through October 31, 2019, and (ii) if any subtenant and sublease are approved by CITY for the Premises and is in good standing regarding its sublease, then CITY will allow the subtenant to remain through October 31, 2019, but that subtenant will then become a tenant of CITY under terms and conditions of a lease similar to the sublease approved by CITY.

Section 1.02 No Extensions.

Requests for continued use of the Premises shall be treated as an application for a new lease and shall require appropriate application to the CITY with all required supporting information and documents, CITY Council approval and the execution of a new CITY lease, containing the then most current terms, covenants, conditions and rent schedules.

Section 1.03 Hold Over.

If TENANT holds the Premises after the expiration of the term of this Lease with the consent of the CITY, express or implied, then such holding over (in the absence of a written agreement between CITY and TENANT with respect thereto) shall be deemed to create a tenancy from month-to-month, terminable on thirty-days' written notice from either Party to the other, at a monthly rental equal to two hundred percent (200%) of the total Rent for the month immediately preceding the expiration of this Lease, and otherwise subject to each and every term, covenant and condition of this Lease.

Section 1.04 Replacement.

As of the Commencement Date of this Lease, this Lease shall extinguish and replace every prior lease between CITY and TENANT respecting the Premises, if any. Any right or interest held by the TENANT pursuant to any existing lease with respect to the Premises which is not granted pursuant to this Lease shall be extinguished as of the Commencement Date of this Lease.

Article 2 RENT

Section 2.01 Annual Minimum Rent.

TENANT agrees to pay to CITY a minimum guaranteed annual rental for the use and occupancy of the Premises in the amount of \$3,000 per month (the "Minimum Rent"), payable in advance commencing on April 1 and then on the first day of each month during the term of this Lease; provided, that the Minimum Rent shall be waived for April and May to the extent TENANT shows proof, satisfactory to the Harbor Director, TENANT has paid, to third parties, at least \$6,000 for necessary cleaning, repair and maintenance to render the currently vacant Premises habitable and rentable. All Rent, including the Minimum Rent and the Percentage Rent, shall be paid in lawful money of the United States of America, without offset or deduction and shall be paid to CITY at the Harbor Department located at 1275 Embarcadero, Morro Bay, California, or at such other place or places CITY may from time to time designate by written notice delivered to TENANT.

Section 2.02 Percentage Rent.

A. In addition to the Minimum Rent, TENANT agrees to pay to CITY at the time and in the manner hereinafter specified, as additional Rent for the use and occupancy of the

Premises, a sum equal to three percent (3%) of TENANT'S Gross Sales, hereinafter defined, less the amount of the Minimum Rent paid pursuant to this Lease (the "Percentage Rent").

B. The term "Gross Sales," as used herein, shall mean (subject to the exceptions and authorized deductions as hereinafter set forth), the total selling price and the total gross amount received by TENANT from all rentals, merchandise sold and services rendered in, on or from the Premises by TENANT, its sublessees, licensees, or concessionaires, both for cash and on credit including, but not limited to, rentals of dockage space, leasing and servicing operations and ticket sales, and if on credit whether or not payment be actually made therefore, all charges for services, alterations or repairs made in or upon the Premises; the gross amount received by TENANT for merchandise sold pursuant to orders received in the Premises, though filled elsewhere; and the gross amount received by TENANT from any and all other sources of income derived from the business conducted upon the Premises.

C. Notwithstanding the other provisions of Section 2.04, the term "Gross Sales" shall not include the following items, and such items may be deducted from Gross Sales to the extent they have been included therein or have been included in a prior computation of Gross Sales or for which a Percentage Rent has been paid under this Lease to CITY:

- (1) Credits and refunds made to customers for merchandise returned or exchanged;
- (2) Any sales or excise taxes otherwise includable in Gross Sales as defined in this Section because such taxes are part of the total selling price of merchandise or services rendered in, from, or on the Premises, where TENANT must account for and remit the taxes to the government entity or entities by which they are imposed; and
- (3) With respect to credit card sales, fees retained or withheld by the issuer and/or merchant bank pursuant to TENANT'S credit card acceptance agreement, and
- (4) Rental payments to TENANT from sublessees whose total gross sales are included in gross sales computations.

D. TENANT shall keep or cause to be kept full, complete, and accurate records, and books of account in accordance with accepted accounting practices showing the total amount of Gross Sales, as defined herein, made each calendar month in, on or from the Premises. TENANT shall keep said records and books of account within San Luis Obispo County and shall notify CITY in advance of their location at all times. Furthermore, TENANT shall at the time of sale and in the presence of the customer cause the full selling price of each piece of merchandise, each rental received, and each service rendered in, on or from the Premises to be recorded in a cash register or cash registers that have cumulative totals and are sealed in accordance with standard commercial practices. Said records, books of account and cash register tapes, including any sales tax reports that TENANT may be required to furnish any government or governmental agency shall at all reasonable times be open to the inspection of CITY, CITY'S auditor, or other

authorized representative or agent of CITY. TENANT consents to the release of sales tax information to CITY and on demand will furnish to CITY a copy of the sales tax reports, quarterly reports and any audit reports of sales for confidential internal use of the CITY in determining Gross Sales for TENANT. TENANT consents and authorizes CITY to request such information directly from the State Board of Equalization or other state agency with which sales tax information is filed.

E. By July 31 of each year, TENANT shall furnish CITY with a statement, to be certified by TENANT as current, true and accurate, which shall set forth the Gross Sales of each department, sublessee, licensee and concession operating in, on or from the Premises for the previous twelve (12) calendar months, ending June 30, just concluded, and the authorized deductions, if any, therefrom; and with it TENANT shall pay to CITY the amount of the Percentage Rent which is due to CITY as shown thereby. If TENANT shall at any time cause an audit of sales of TENANT'S business to be made by a public accountant, TENANT shall furnish CITY with a copy of said audit without cost or expense to CITY. CITY may, once in any twelve-month period, cause an audit of the business of TENANT to be made by a public accountant of CITY'S own selection. TENANT shall, upon receiving written notice of CITY'S desire for such an audit deliver and make available all such books, records and cash register tapes to the public or certified public accountant selected by CITY. Furthermore, TENANT shall promptly on demand reimburse CITY for the full cost and expense of said audit, should the audit disclose that the questioned statement or statements understated Gross Sales by five percent (5%) or more but less than ten percent (10%). In the event that an audit performed at CITY'S request discloses that TENANT understated Gross Sales by less than 5%, the cost of such audit shall be paid by CITY. In the event that any audit or other review of records discloses that the amounts reported as Gross Sales was understated by TENANT by ten percent (10%) or more, CITY shall not only be entitled to recover from TENANT all costs of audit and review but shall also be entitled to recover from TENANT a penalty equal to two times the Percentage Rent due pursuant to this Lease on such unreported amounts. Whenever any audit discloses that Gross Sales were understated by any amount, TENANT shall immediately pay the additional Percentage Rent therein shown to be payable by TENANT to CITY, together with interest at the Default Rate thereon, from the date the Percentage Rent was payable until the date paid.

F. CITY shall be entitled at any time within five (5) years after the receipt of any such Percentage Rent payment, to question the sufficiency of the amount thereof and/or the accuracy of the statement or statements furnished by TENANT to justify the same. For the purpose of enabling CITY to check the accuracy of any such statement or statements, TENANT shall for said period of five (5) years after submission to CITY of any such statement keep all of TENANT'S records, including sales tax returns, all cash register tapes and other data which in

any way bear upon or are required to establish in detail TENANT'S Gross Sales and any authorized deductions therefrom as shown by any such statements and shall upon request make the same available to CITY for examination.

Section 2.03 Reimbursements.

If TENANT fails to perform any term or covenant of this Lease, CITY may, but is not obligated to, perform such term or covenant, and TENANT shall reimburse CITY therefore as additional Rent hereunder. As an illustration and not as a limitation, if TENANT fails to procure the insurance required by this Lease, CITY may, but is not obligated to, obtain such insurance, with the cost of the premiums being due to CITY upon demand as additional Rent.

Section 2.04 Penalty and Interest.

(1) If any Rent is not received within ten (10) days following the date on which the Rent first became due, TENANT shall pay a late penalty of ten percent (10%) of the amount of the Rent in addition to the Rent.

(2) In addition to the penalty, TENANT shall pay interest at the rate of one percent (1%) per month or fraction thereof or the maximum amount permitted by law as of the date this Lease is signed, whichever is greater (the "Default Rate"), on the amount of the Rent, exclusive of the penalty, from the date on which Rent first became delinquent until paid. The term "Rent" includes any sums advanced by the CITY and any unpaid amounts due from TENANT to the CITY.

Article 3 USE OF PREMISES

Section 3.01 Permitted Uses.

The Premises shall, during the term of this Lease, be used for the purpose of operating and conducting thereon and therein the uses permitted by, and in compliance with, all Conditional Use Permits applicable to the Premises, as may be amended from time to time, and for no other purpose. At the commencement date of this Lease, such uses include Restaurant, bar, retail sales, docks for commercial and pleasure boats, seafood market and office space.

Section 3.02 Unauthorized Use.

TENANT agrees to allow only those uses authorized in Section 3.01 hereinabove and any unauthorized use thereof shall constitute a breach of this Lease and shall, at the option of CITY, terminate this Lease.

Section 3.03 Operation of Business - Hours of Operation.

Failure to actively and diligently conduct the business authorized herein constitutes a breach of the agreement and shall, at the option of CITY, terminate this lease.

(1) TENANT shall during the term of this Lease conduct retail sales business of the nature specified in Section 3.01 of this Lease in the downstairs portion of the Premises in an efficient and diligent manner and keep the Premises open for the conduct of business continuously and without interruption for at least six hours each day of the year except one day each week and legal holidays. This provision shall not apply if the Premises shall be closed and the business of TENANT is temporarily shut down for a period not to exceed fourteen (14) calendar days in any calendar year to make necessary repairs, maintenance or other construction deemed necessary by TENANT. This provision shall not apply if the Premises shall be closed and the business of TENANT is temporarily shut down as authorized or required by the CITY Manager or on account of strikes, walkouts, or causes beyond the control of TENANT or for not more than three (3) days out of respect to the memory of an officer, employee, or close relative of any officer or employee of TENANT.

(2) TENANT shall operate TENANT'S business on the Premises with due diligence and efficiency and in like manner as comparable businesses operated in the CITY or the coastal area of San Luis Obispo County, so as to produce the maximum amount of Gross Sales and gross receipts from services which may be produced from TENANT'S business; and TENANT at all times shall carry on Premises, a stock or merchandise of such size, character, and quality as is reasonable, designed to produce the maximum return to TENANT, when the sale of merchandise is a permitted use under this Lease.

Notwithstanding the foregoing, CITY understands and agrees the portions of the Premises which were formerly occupied by Off the Hook restaurant (the "Restaurant Space"), and the upstairs spaces, are now vacant and in need of rehabilitation before they can be properly occupied. Based on that, CITY agrees TENANT will use its best good faith effort to do what is necessary to make those areas usable, as soon as possible. CITY and TENANT also agree if that is not possible, then TENANT shall at least do the following:

(1) Repair, as needed, and maintain the two restrooms for public use during regular business hours for the Restaurant Space; provided, that if the Parties agree the restrooms can be safely cordoned off from the rest of the Restaurant Space, then the restricted access shall be installed and maintained by TENANT and the two restrooms shall be open for public use during the

regular business hours for the downstairs portion of the Premises currently occupied by Under the Sea Gallery,

- (2) Allow the use of the patio/open air portions of that area to be used by the public similar to the Harbor Walk and
- (3) Improve, to the reasonable approval of the Harbor Director, the aesthetics, housekeeping and utility of all the publicly viewable portions of the façade areas and common public open spaces on the Premises.

Section 3.04 Competition.

During the term of this Lease, TENANT shall not directly nor indirectly acquire or establish any similar or competing business within a radius of five (5) miles from the location of the Premises; provided, however, that TENANT may, with prior written approval from CITY, own or operate more than one business, whether or not competing and similar along the Embarcadero upon CITY lease sites. The purpose of this Section is to prevent and prohibit TENANT from reducing revenue to CITY by diverting business from the operation at the Premises to another similar business owned by TENANT within the CITY, but not upon a CITY lease site from which CITY is paid rent based on Gross Sales. In accordance with this Section, CITY hereby approves TENANT'S current operations at 725 Embarcadero (Rose's Landing).

Section 3.05 Hazardous Materials.

(1) TENANT shall not transport, use, store, maintain, generate, dispose, release, treat or discharge any "Hazardous Material" (as defined below) upon or about the Premises (such activities being hereafter referred to as "Hazardous Materials Activities"), nor permit TENANT'S employees, agents, or contractors to engage in Hazardous Materials Activities upon or about the Premises, except as allowed by applicable law. The term "Hazardous Material" for purposes hereof shall mean any chemical, substance, material or waste or component thereof which is now or hereafter listed, defined or regulated as a hazardous or toxic chemical, substance, material or waste or component thereof by any federal, state or local governing or regulatory body having jurisdiction, or which would trigger any employee or community "right-to-know" requirements adopted by any such body. All Hazardous Materials Activities at the Premises shall be conducted strictly in accordance with all applicable laws and regulations. If TENANT shall transport any hazardous waste from the Premises, then such transportation shall be done only by a contractor duly licensed to haul hazardous waste and shall use only a duly licensed disposal site approved by TENANT'S liability insurer.

(2) TENANT shall promptly notify CITY of: (i) any enforcement, cleanup or other regulatory action taken or threatened by any governmental or regulatory authority with respect to

the presence of any Hazardous Material on the Premises or the migration thereof from or to other property, (ii) any demands or claims made or threatened by any party against TENANT or the Premises relating to any loss or injury resulting from any Hazardous Material on or from the Premises, and (iii) any matters where TENANT is required by applicable law to give a notice to any governmental or regulatory authority respecting any Hazardous Material on the Premises. CITY shall have the right (but not the obligation) to inspect the Premises, to take such remedial action on the Premises, as CITY may deem appropriate, and to join and participate, as a party, in any legal proceedings or actions affecting the Premises initiated in connection with any environmental, health or safety law.

(3) If any Hazardous Material is released, discharged or disposed of by TENANT or its employees, agents or contractors, on or about the Premises in violation of the foregoing provisions, then TENANT shall immediately notify CITY. CITY may elect either to take such remedial action as CITY deems appropriate, in which event TENANT shall reimburse CITY for all costs thereof within ten (10) days after demand, or direct TENANT to perform such remediation. If CITY directs TENANT to perform the remediation, then TENANT shall immediately take such remedial action, as CITY shall direct. TENANT shall, properly and in compliance with applicable laws clean up and remove the Hazardous Material from the Premises and any other affected property at TENANT'S expense. If CITY directs TENANT to perform remediation hereunder and if TENANT shall fail to comply with the provisions of this Section within five (5) days after written notice by CITY, or such shorter time as may be required by applicable law or in order to minimize any hazard to persons or property, then CITY may (but shall not be obligated to) arrange for such compliance directly or as TENANT'S agent through contractors or other parties selected by CITY at TENANT'S expense (without limiting CITY'S other remedies under this Lease or applicable law).

Section 3.06 Tidelands Trust.

TENANT shall use and occupy the Premises in strict compliance with the Tidelands Trust purposes under which the Premises or any portion thereof are held by CITY pursuant to the grants from the State of California as set forth in this Lease.

Section 3.07 Compliance with Law.

TENANT shall, at no cost to CITY, comply with all of the requirements of all local, municipal, county, state and federal authorities now in force, or which may hereafter be in force, pertaining to the Premises, and shall faithfully observe in the use of the Premises all local, municipal and county ordinances and state and federal statutes, rules, regulations and orders now

in force or which may hereafter be in force (collectively, "Legal Requirements") provided that TENANT shall not be required to comply with any Legal Requirement imposed by the CITY that would substantially deprive TENANT of a material benefit under this lease unless such Legal Requirement has been imposed or required by a county, state or federal authority. The judgment of any court of competent jurisdiction, or the admission of TENANT in any action or proceeding against TENANT, whether CITY is a party thereto or not, TENANT has violated any such Legal Requirement in the use of the Premises shall be conclusive of that fact as between CITY and TENANT.

Section 3.08 Waste or Nuisance.

TENANT shall not commit or permit the commission by others of any waste on the Premises; TENANT shall not maintain, commit, or permit the maintenance or commission of any nuisance as defined by law on the Premises; and TENANT shall not use or permit the use of the Premises for any unlawful purpose.

Section 3.09 Use by CITY.

(1) Subject to TENANT's rights hereunder to possession of the Premises, CITY may grant licenses to, or otherwise authorize, other persons and entities permitting uses of the Morro Bay Harbor.

(2) CITY also retains and reserves for itself, its successors and assigns, all oil, gas, petroleum and other mineral or hydrocarbon substances in and under the lands leased hereby together with right to prospect and extract all such substances.

Article 4 CONSTRUCTION, ALTERATION AND REPAIRS

Section 4.01 Construction Approval.

(1) TENANT shall not make or permit any other person to make any alterations or structural additions or structural modifications to the Premises or to any structure thereon or facility appurtenant thereto if the cost thereof shall exceed ten thousand dollars (\$10,000), without the prior written consent of CITY. The consent to be obtained pursuant to this Section 4.01(1) shall be requested from the Harbor Director, or the City's designee, for CITY. If the Harbor Director or any future successor to the duties of the City's Harbor Director, or the City's designee, gives such consent to proceed, it is understood that such consent is given by CITY only in its capacity as the landlord under this Lease and not as the permit-issuing

authority. TENANT remains obligated to obtain any needed building permits and comply with all applicable planning processes.

(2) Where required by the Morro Bay Municipal Code, California Coastal Act, Corps of Engineers or any other state or federal agency having authority over the proposed project, then all Conditional Use Permits, Concept Plans, Precise Plans, Coastal Development Plans, and any other required plans or permits shall be applied for and approved prior to any construction, alteration or repairs.

Section 4.02 Construction Bond.

(1) Prior to the commencement of any construction the cost of which is greater than the amount of one hundred thousand dollars (\$100,000), TENANT shall file with the Morro Bay CITY Clerk a final detailed Civil Engineer's, Registered Architect's or Licensed and Bonded General Contractor's estimate of the cost of construction and installation of improvements on the Premises. Said estimate must be submitted to the CITY Engineer for approval. TENANT shall file with the Morro Bay CITY Clerk a faithful performance bond, in a form and issued by a corporate surety company satisfactory to CITY, in an amount satisfactory to CITY but not in excess of one hundred percent (100%) of the final detailed cost estimate, securing the faithful performance of TENANT or its contractor in the completion of said construction.

(2) TENANT shall also file with the Morro Bay CITY Clerk a labor and materials bond, in a form and issued by a corporate surety company satisfactory to CITY, in an amount satisfactory to CITY but not in excess of one hundred percent (100%) of the final detailed cost estimate, securing the payment of all claims for the performance of labor or services on, or the furnishing of materials for, the performance of said construction.

(3) In lieu of the above referenced bonds, TENANT may post cash deposits or may make other mutually satisfactory arrangements to guarantee the completion of construction projects. In the event the contractor bonds the project, CITY may be named as additional indemnitee to comply with these requirements.

Section 4.03 Mechanics' Liens.

At all times during the term of this Lease, TENANT shall keep the Premises and all buildings, installations and other improvements now or hereafter located on the Premises free and clear of all liens and claims of liens for labor, services, materials, supplies, or equipment performed on or furnished to the Premises. TENANT further agrees to at all times, save CITY free and harmless and indemnify CITY against all claims for labor or materials in connection with any improvement, repairs, or alterations on the Premises, and the cost of defending against

such claims, including reasonable attorneys' fees. Should TENANT fail to pay and discharge or cause the Premises to be released from such liens or claim of liens within ten (10) days after the filing of such lien or levy, TENANT shall upon written notification be required to immediately deposit with CITY a bond conditioned for payment in full of all claims on which said lien or levy has been filed. Such bond shall be acknowledged by TENANT as principal and by a company or corporation, licensed by the Insurance Commissioner of the State of California to transact the business of a fidelity and surety insurance company as surety. The beneficiary of any security instrument which instrument is on record with CITY, shall have the right to file such a bond on behalf of TENANT. CITY shall have right to post and keep posted on the Premises notices of non-responsibility and any other notices that may be provided by law or which CITY may deem proper for the protection of CITY and Premises from such liens. TENANT shall give CITY notice at least twenty (20) days prior to commencement of any work on the Premises to afford CITY the opportunity to post such notices.

Section 4.04 Ownership of Improvements.

The Parties agree title to all buildings, structures, installations and improvements of any kind or other property on the Premises, however occurring, vests in CITY, with the exception of trade fixtures, appliances, machines or other personal property (i) installed on Premises by TENANT and (ii) to which CITY and TENANT, agree to in writing prior to installation, title is vested in TENANT. The Parties agree, at the termination of this Lease, however occurring, TENANT shall have sixty (60) days thereafter to remove from the Premises all trade fixtures, appliances and machines installed on Premises by TENANT and other personal property title of which is vested in TENANT, as provided hereunder, (TENANT Property). If TENANT fails to remove from the Premises any TENANT Property as required by the previous sentence, then title to the TENANT Property not so removed shall vest in CITY and TENANT shall not remove same.

Article 5 LEASEHOLD MORTGAGES

TENANT shall not mortgage, securitize or hypothecate this leasehold interest in whole or any part without the prior written approval of CITY as evidenced by a resolution of the City Council of CITY.

Article 6 REPAIRS, MAINTENANCE AND RESTORATION

Section 6.01 Maintenance by TENANT.

At all times during the term of this Lease, TENANT shall, at TENANT'S own cost and expense, keep and maintain all improvements now or hereafter on the Premises in good order and repair and in a safe and clean condition; provided, that CITY shall be responsible for repair, CITY determines are necessary, of any seawalls, revetments or bulkheads on the Premises. Furthermore, TENANT shall, at TENANT'S own cost and expense, maintain at all times during the term of this Lease the whole of the Premises in a clean, sanitary, neat and orderly condition. CITY may, at the sole option of CITY, clean and clear the Premises, at TENANT'S cost and expense, in the event TENANT fails to clean and clear the Premises in accordance with this Section to the satisfaction of CITY after fifteen (15) days' written notice to TENANT from CITY of CITY'S intent to exercise this option.

Section 6.02 Legal Requirements.

At all times during the term of this Lease, TENANT, at no cost to CITY, shall:

(1) Make all alterations, additions, or repairs to the Premises or the improvements or facilities on the Premises required by any Legal Requirements (as defined in Section 3.07 above) now or hereafter made or issued;

(2) Observe and comply with all Legal Requirements now or hereafter made or issued respecting the Premises or the improvements or facilities located thereon;

(3) Obtain all required permits pursuant to the Morro Bay Municipal Code or State law prior to the initiation of any repair or maintenance activity; and

(4) Indemnify and hold CITY and the property of CITY, including the Premises, free and harmless from any and all liability, loss, damages, fines, penalties, claims and actions resulting from TENANT'S failure to comply with and perform the requirements of this section.

Section 6.03 Failure to Repair.

In the event failure to repair results in a hazardous or unsafe condition, CITY shall have the right and option but not the obligation to close and prohibit access to the unsafe portion of the Premises until such repairs are completed and accomplished and the Premises rendered safe for public use. In addition, if TENANT fails to repair any hazardous or unsafe condition within ten (10) days of written notice thereof from CITY, CITY shall have the right, but not the obligation, to perform such repair at TENANT'S expense. TENANT shall reimburse CITY for any such repair undertaken by CITY, promptly upon CITY'S demand, as additional Rent. Failure by

CITY to enforce any of the provisions of this Article shall not constitute a waiver of these provisions and CITY may at any time enforce all of the provisions of this Article, requiring all necessary repairs, rebuilding or replacement.

Section 6.04 Inspection by CITY.

CITY or CITY'S agents, representatives, or employees may enter the Premises at all reasonable times for the purpose of inspecting the Premises to determine whether TENANT is complying with the terms of this Lease and for the purpose of doing other lawful acts that may be necessary to protect CITY'S interest in the Premises under this Lease or to perform CITY'S duties under this Lease.

Section 6.05 TENANT'S Duty to Restore Premises.

(1) If at any time during this Lease, any improvements now or hereafter on the Premises are damaged or destroyed in whole or in part by the elements, or any other cause not the fault of TENANT or CITY and such destruction makes uninhabitable, any portion of the Premises at which TENANT or its sublessees are located, as reasonably determined by CITY'S Building Official, then this Lease shall terminate upon written notice from either Party.

(2) Any and all insurance proceeds that become payable at any time during the term of this Lease because of damage to or destruction of any improvements on the Premises shall be paid to CITY, except for those proceeds payable for TENANT Property.

Article 7 INDEMNITY AND INSURANCE

Section 7.01 Indemnity Agreement.

(1) TENANT shall indemnify and hold CITY, and the property of CITY (including the Premises and any improvements now or hereafter on the Premises), and the CITY'S officers, officials, employees and volunteers harmless from any and all liability, claims, loss, damages, and expenses, including attorney fees and litigation expenses, resulting from TENANT'S occupation and use of the Premises or any negligent act or omission of the TENANT or any of its subtenants, employees, contractors or anyone for whom TENANT may be liable, specifically including, without limitation, any liability, claim, loss, damage, or expense arising by reason of:

(a) The death or injury of any person, including TENANT or any person who is an employee or agent of TENANT, or by reason of the damage to or destruction of any property, including property owned by TENANT or by any person who is an employee or agent of TENANT, from any cause whatever while such person or property is in or on the Premises or

in any way connected with the Premises or with any of the improvements or personal property on the Premises;

(b) The death or injury of any person, including TENANT or any person who is an employee or agent of TENANT, or by reason of the damage to or destruction of any property, including property owned by TENANT or any person who is an employee or agent of TENANT, caused or allegedly caused by either (i) the condition of the Premises or any improvement placed on the Premises by TENANT, or (ii) any act or omission on the Premises by TENANT or any person in, on, or about the Premises with or without the permission and consent of TENANT;

(c) Any work performed on the Premises or materials furnished to the Premises at the instance or request of TENANT or any person or entity acting for or on behalf of TENANT;

(d) TENANT'S failure to perform any provision of this Lease or to comply with any Legal Requirement imposed on TENANT or the Premises.

(2) TENANT'S obligations pursuant to this Section to indemnify and hold harmless do not extend to any liability, claim, loss, damage or expense arising from CITY'S active negligence or willful misconduct.

Section 7.02 Liability Insurance.

During the term of this Lease, TENANT shall maintain at its cost Commercial General Liability insurance with coverages at least as broad as ISO Forms labeled "City of Morro Bay Insurance requirements for Lessees", Certificate of Insurance – City of Morro Bay", and "Additional Insureds – Managers or Lessors of Premises" attached hereto as Exhibit B and made a part hereof as may be updated or changed from time to time at the sole discretion of the CITY, insuring against claims for bodily injury (including death), property damage, contractual liability, personal injury and advertising injury occurring on the Premises or from operations located in any part of the Premises. Such insurance shall afford protection in amounts no less than One Million Dollars (\$1,000,000) per occurrence for bodily injury, personal injury and property damage, provided that if insurance with a general aggregate limit is used, either the general aggregate limit shall apply separately to the Premises or the general aggregate limit shall be twice the occurrence limit stated in this Section. All liability insurance carried by TENANT hereunder shall name CITY, its officers, officials, employees and volunteers as additional insureds, and shall be primary insurance with respect to such additional insureds. TENANT shall include all its subtenants as insureds under TENANT's liability policies or shall furnish

separate certificates and endorsements for each subtenant. All coverages for subtenants shall comply with all requirements of this Article Seven.

Section 7.03 Worker's Compensation.

TENANT shall maintain at TENANT'S own expense and keep in full force and effect during the term of this Lease, Worker's Compensation Insurance as provided by law. Said insurance shall contain a waiver of subrogation rights against CITY. TENANT shall also maintain employer's liability insurance with minimum coverage of \$1,000,000 per accident for bodily injury or disease.

Section 7.04 Property Insurance.

TENANT shall, at its cost, at all times during the term of this Lease keep all improvements and other structures on the Premises, as well as any and all additions, improvements and betterments thereto, insured for one hundred percent (100%) of their full replacement cost with no co-insurance provision against loss or destruction by the perils covered by "all risk" (excluding earthquake) property damage insurance policies. Any loss payable under such insurance shall be payable to TENANT, CITY, and any Lender under a Leasehold Encumbrance pursuant to Article 5 of this Lease, as their interests may appear, and such proceeds shall be used and applied in the manner required by Article 6 of this Lease.

Section 7.05 Additional Coverage.

TENANT shall also maintain, at its expense, the insurance described in this Section 7.05.

(1) If TENANT has (or is required by any Legal Requirement to have) a liquor license and is selling or distributing alcoholic beverages on the Premises, then TENANT shall maintain liquor liability coverage in appropriate amounts. TENANT shall require any subtenant who has (or is required by any Legal Requirement to have) a liquor license and who is selling or distributing alcoholic beverages on the Premises, to maintain such coverage.

(2) TENANT shall maintain "all risk" (excluding earthquake) property damage insurance covering TENANT's personal property located at the Premises, in amounts not less than the full replacement value of such personal property. CITY shall have no interest in the proceeds of such insurance.

(3) TENANT shall, at TENANT's own expense, obtain and maintain any additional insurance coverages that CITY may reasonably require. As illustration only and not as a limitation, in appropriate circumstances such additional insurance may include increased general

liability limits, business interruption coverage, business automobile liability, boiler and machinery insurance and/or builder's risk insurance. However, TENANT shall not be required to maintain additional coverages that are in excess of those typically maintained by similarly situated tenants in the Morro Bay area.

Section 7.06 General Requirements.

Except as specifically provided to the contrary, all the insurance required pursuant to this Article Seven shall be subject to the requirements of this Section 7.06.

(1) Maintenance of proper insurance coverage is a material element of this Lease and failure to maintain or renew coverage or to provide evidence of coverage and/or renewal may be treated by the CITY as a material breach of contract. TENANT shall forward the CITY specifications and forms to TENANT'S insurance agent for compliance.

(2) CITY may at any time require TENANT to increase the minimum coverage limits for insurance required by this Lease, but every such increase shall be reasonable under the circumstances.

(3) All policies shall be issued by insurance companies authorized to issue such insurance in California, with an A.M. Best's rating of no less than A: VII.

(4) Any deductibles or self-insured retentions must be declared to and approved by CITY. At the option of CITY, either: the insurer shall reduce or eliminate such deductibles or self-insured retentions as respects CITY, its officers, officials, employees and volunteers; or the TENANT shall provide a financial guarantee satisfactory to CITY guaranteeing payment of losses and related investigations, claim administration and defense expenses.

(5) Each insurance policy required by this Lease shall be endorsed to state that coverage shall not be cancelled or reduced, except after thirty (30) days' prior written notice by certified mail, return receipt requested, has been given to CITY.

(6) TENANT shall furnish CITY with certificates and amendatory endorsements effecting the coverage required by this Lease. The endorsements shall be on forms provided by CITY or on other than CITY's forms, provided those endorsements or policies conform to the requirements. All certificates and endorsements are to be received and approved by CITY before use of the Premises, and promptly following any renewal or replacement. CITY reserves the right at any time to require complete, certified copies of all required insurance policies, including endorsements effecting the coverage required by these specifications.

(7) TENANT's insurance coverage shall be primary insurance as respects CITY, its officers, officials, employees, and volunteers. Any insurance or self-insurance maintained by CITY, its officers, officials, employees, or volunteers shall be excess of TENANT's insurance and shall not contribute with it.

Section 7.07 No Subrogation.

TENANT agrees that in the event of loss due to any of the perils for which it has agreed to provide insurance, TENANT shall look solely to its insurance for recovery. TENANT hereby grants to the CITY, on behalf of any insurer providing insurance to either TENANT or CITY with respect to TENANT'S occupancy of the Premises, a waiver of any rights to subrogation which any such insurer of said TENANT may acquire against the CITY by virtue of the payment of any loss under such insurance. Each insurance policy required under this Lease including those insuring TENANT against claims, expense, or liability for injury to persons or property shall provide that the insurer shall not acquire by subrogation any right to recovery which TENANT has expressly waived in writing prior to the occurrence of the loss.

Section 7.08 TENANT'S Waiver.

TENANT hereby waives any right of recovery against CITY for each claim, expense, liability, or business interruption, or other loss, except where caused by CITY'S active negligence or willful misconduct. TENANT agrees that to the extent that TENANT fails to acquire insurance, TENANT shall not have any claim against CITY for any loss that results from a risk or peril that would have been included in such insurance.

Section 7.09 Insurance Not a Limit.

The insurance requirements of this Article Seven are independent of, and do not limit or modify, TENANT'S indemnification and other obligations pursuant to this Lease.

Article 8 TAXES AND FEES

Section 8.01 TENANT to Pay Taxes.

TENANT shall pay, before delinquency, all taxes and assessments levied upon or assessed to TENANT on the Premises by reason of this Lease or of any equipment, appliances, improvement, or other development of any nature whatsoever, erected, installed, or maintained by TENANT or by reason of the business or other activity of TENANT upon or in connection with the Premises. TENANT shall pay all possessory interest taxes applicable to the Premises.

Section 8.02 TENANT to Pay License and Permit Fees.

TENANT shall pay any fees imposed by law for licenses or permits for any business or activities including construction by TENANT upon the Premises.

Section 8.03 Utilities.

TENANT shall pay, or cause to be paid, and hold CITY and the property of CITY, including the Premises, free and harmless from all charges for the furnishing of gas, water, electricity, telephone service, and for other public utilities to the Premises during the term of this Lease and for the removal of garbage and rubbish from the Premises during the term of this Lease.

Article 9 CONDEMNATION

Section 9.01 Total Condemnation.

If title and possession to all of the Premises is permanently taken for any public or quasi-public use under any statute, or by the right of eminent domain, then this Lease shall terminate on the date that possession of the Premises is taken, and both CITY and TENANT shall thereafter be released from all obligations, including Rent, all of which shall be prorated to the date of termination, except those specified in Section 9.02 of this Lease.

Section 9.02 Condemnation Award.

Any compensation or damages awarded or payable because of the permanent taking of all or any portion of the Premises by eminent domain shall be allocated between CITY and TENANT as follows:

(1) All compensation or damages awarded or payable for the taking by eminent domain of any land that is part of the Premises shall be paid to and be the sole property of CITY free and clear of any claim of TENANT or any person claiming rights to the Premises through or under TENANT.

(2) All compensation or damages awarded or payable which is specifically attributed by the taking party to the "good will" of TENANT'S business shall be paid to and be the sole property of TENANT.

(3) All compensation or damages awarded or payable because of any improvements constructed or located on the portion of the Premises taken by eminent domain where only a portion of the Premises is taken by eminent domain, and TENANT is not entitled to or does not

terminate this Lease, shall be applied in the manner specified in Section 9.04 toward the replacement of such improvements with equivalent new improvements on the remaining portions of the Premises.

(4) All compensation or damages awarded or payable because of any improvements constructed or located on the portion of the Premises taken by eminent domain where this Lease is terminated because of the taking by eminent domain, whether all or only a portion of the Premises is taken by eminent domain, shall be allocated between CITY and TENANT as follows:

(a) That percentage of the compensation or damages awarded or payable because of the improvements that equals the percentage of the full term of this Lease that has, at the time of the taking, not expired shall belong to and be the sole property of TENANT.

(b) That percentage of the compensation or damages awarded or payable because of the improvements that equals the percentage of the full term of this Lease that has, at the time of the taking, expired shall belong to and be the sole property of CITY.

(c) The term "time of taking" as used in this Section shall mean 12:01 a.m. of the date that the agency or entity exercising the eminent domain power, takes, title, or the date that it takes physical possession of the portion of the Premises, whichever shall first occur.

(5) Any severance damages awarded or payable because only a portion of the Premises is taken by eminent domain shall be the sole and separate property of CITY.

Section 9.03 Termination for Partial Taking.

If, during the term of this Lease, title and possession of only a portion of the Premises is taken for any public or quasi-public use under any statute, or by right of eminent domain, then TENANT may, at TENANT'S option, terminate this Lease by serving written notice of termination on CITY within ninety (90) days after TENANT has been deprived of actual physical possession of the portion of the Premises taken for such public use. This Lease shall terminate on the first day of the calendar month following the calendar month in which the notice of termination described in this section is served on CITY. On termination of this Lease pursuant to this Article, all subleases and subtenancies in or on the Premises or any portion of the Premises created by TENANT under this Lease shall also terminate and the Premises shall be delivered to CITY free and clear of all such subleases and subtenancies, provided, however, that CITY may, at CITY'S option, by mailing written notice to a subtenant allow any subtenant to attorn to CITY and continue such subtenant's occupancy on the Premises as a TENANT of

CITY. On termination of this Lease pursuant to this section, however, both CITY and TENANT shall be released from all obligations under this Lease, except those specified in Section 9.02 of this Lease.

Section 9.04 Rent Abatement for Partial Taking.

If, during the term of this Lease, title and possession of only a portion of the Premises is taken under the power of eminent domain by any public or quasi-public agency or entity and TENANT does not terminate this Lease, then this Lease shall terminate as to the portion of the Premises taken under eminent domain on the date actual physical possession of the portion taken by eminent domain is taken by the agency or entity exercising the eminent domain power. Furthermore, the Rent payable under this Lease shall, as of that time be reduced in the same proportion of the Premises taken by eminent domain bears to the full value of the Premises at that time; provided however, that TENANT shall make a good faith effort to replace any improvements or facilities with equivalent new facilities on the remaining portion of the Premises and do all other acts at TENANT'S own cost and expense required by the eminent domain taking to make the remaining portion of the Premises fit for the use specified in this Lease.

Section 9.05 Conveyance in Lieu of Eminent Domain.

A voluntary conveyance by CITY, with the consent of TENANT, of title to all or a portion of the Premises to a public or quasi-public agency or entity in lieu of and under threat by such agency or entity to take the same by eminent domain proceedings shall be considered a taking of title to all or such portion of the Premises under the power of eminent domain subject to the provisions of this Article.

Section 9.06 Temporary Taking.

If the possession of the Premises or any portion thereof should be taken under the power of eminent domain by any public or quasi-public agency or entity for a limited period not extending beyond the term of this Lease, then this Lease shall not terminate (except as provided in this Section 9.06) and TENANT shall continue to perform all its obligations hereunder, except only to the extent that TENANT is prevented from performing such obligations by reason of such taking. TENANT shall be entitled to receive the entire amount of compensation or damages awarded because of such temporary taking. If a temporary taking extends for more than thirty-six (36) months, then TENANT shall have the right to terminate this Lease, and TENANT shall be entitled to receive, out of the compensation or damages awarded because of

such temporary taking, the amount that is attributable to the period of time up until the effective date of TENANT'S termination of this Lease.

Article 10 ASSIGNMENT AND SUBLEASING

Section 10.01 No Assignment Without CITY'S Consent.

Except as provided in this Article 10, TENANT shall not assign or otherwise transfer this Lease, any right or interest in this Lease, or any right or interest in the Premises or any of the improvements that may now or hereafter be constructed or installed on the Premises without the express written consent of CITY evidenced by resolution first had and obtained. Any assignment or transfer by TENANT without the prior written consent of CITY, whether it be voluntary or involuntary, by operation of law or otherwise, is void and shall, at the option of CITY, terminate this Lease. A consent by CITY to one assignment shall not be deemed to be a consent to any subsequent assignment of this Lease by TENANT. CITY shall not unreasonably nor arbitrarily withhold its approval to the assignment or transfer of this Lease to an assignee who is financially reliable and qualified to conduct the business for which this Lease was granted. It is mutually agreed TENANT'S qualifications are a part of the consideration for granting of this Lease and TENANT does hereby agree to maintain active control and supervision of the operation conducted on the Premises.

Section 10.02 Change of Ownership as Assignment.

For purposes of this Article 10, the following transactions will be deemed to be assignments or transfers:

(1) If TENANT is a partnership or limited liability company:

(a) A change in ownership effected voluntarily, involuntarily, or by operation of law, within a twelve-month (12-month) period, of twenty-five percent (25%) or more of the partners or members or twenty-five percent (25%) or more of the partnership or membership interests; or

(b) The dissolution of the partnership or limited liability company without its immediate reconstitution.

(2) If TENANT is a closely held corporation (i.e., one whose stock is not publicly held and not traded through an exchange or over the counter):

(a) The sale or other transfer, within a twelve-month (12-month) period, of more than an aggregate of twenty-five percent (25%) of the voting shares of TENANT (other than to immediate family members by reason of gift or death); or

(b) The dissolution, merger, consolidation, or other reorganization of TENANT.

Section 10.03 Application for Assignment.

A condition of an assignment shall be that TENANT shall file with the CITY an application to assign the leasehold prepared by the prospective assignee. Concurrently with filing the application, TENANT shall pay a reasonable fee associated with the cost of processing said application, in cash or certified or cashier's check to enable CITY adequately to investigate the proposed assignee's qualifications as a permitted assignee. CITY shall not be required to account for the use of the sum paid. If the proposed assignee's net worth on the date of assignment is not sufficient to reasonably guarantee successful operation of the Premises in compliance with all applicable CITY, County, State and federal requirements, CITY may withhold approval of the assignment or condition it upon TENANT'S guarantee of such assignee's obligations hereunder for such period as CITY deems advisable. Net worth shall mean the amount by which the total of all assets shall exceed the total of all liabilities as determined in accordance with general accepted accounting principles as approved by CITY'S auditor, or other authorized representative or agent.

Section 10.04 Probate Transfer of Assignment.

If TENANT is an individual, nothing herein contained will prevent the transfer of this Lease by will, or by operation of law under the intestacy provisions of the California Probate Code as it may be amended from time to time. Probate sale of the leasehold interest will not be permitted without the consent of the CITY, evidenced by resolution, first had and obtained.

Section 10.05 No Sublease Without CITY'S Consent.

TENANT shall not sublease the whole nor any part of the Premises, or license, permit, or otherwise allow any other person (the employees of TENANT excepted) to occupy or use the Premises, or any portion thereof, without the prior written consent of CITY'S Harbor Director, or any future successor to the duties of the City'S Harbor Director. A consent to one subletting, occupation, licensing or use shall not be deemed to be a consent to any subsequent subletting, occupation, licensing or use by another person. Any sublease or license without CITY'S written consent shall be void, and shall at CITY'S option, terminate this Lease. CITY shall not

unreasonably nor arbitrarily withhold its consent to sublet to one who is qualified and financially reliable. CITY'S consent to any occupation, use, or licensing shall be in CITY'S sole and absolute discretion. Notwithstanding any provisions herein to the contrary, the terms "assignment," "subletting," "occupation," or "use," shall not be construed or interpreted to mean or include the temporary, short term renting or leasing of boat slips, motel, hotel, or apartment accommodations on the premises.

Section 10.06 Subtenant Subject to Lease Terms.

Any and all subleases shall be expressly made subject to all the terms, covenants, and conditions of this Lease. Subject to Section 1.01, the term of any sublease shall not extend beyond the term of this Lease. Subject to Sections 1.01 and 10.09, termination of this Lease prior to the expiration of this Lease term shall also terminate any and all subleases. A breach of the terms of this Lease by a subtenant shall constitute a breach on the part of TENANT and shall subject both the subtenant and TENANT to all the remedies provided to CITY herein and by law. Failure by any subtenant to report Gross Sales or to pay Percentage Rent due from subtenant shall constitute a breach of this lease. TENANT hereby agrees to and does guarantee payment of such Percentage Rent due by a subtenant under the terms of this lease.

Section 10.07 Consent Form Agreement.

Prior to any consent by CITY'S Harbor Director to any sublease hereof, TENANT shall cause to be executed between TENANT and any subtenant an agreement making the CITY a third-party beneficiary, in a form acceptable to CITY'S Harbor Director, whereby the subtenant agrees to be bound by all of the terms, covenants and conditions of this Lease. Further, it is agreed by TENANT any default by the subtenant of any of the terms, covenants and conditions of this Lease shall be deemed to be violations by TENANT of this Lease and that all remedies of CITY for such violation, including termination of this Lease, shall immediately be enforceable by CITY against TENANT. TENANT shall apply any and all monies received from any subtenant first to the payment of obligations of the subtenant to CITY.

Section 10.08 TENANT and Guarantor Remain Liable.

Prior to approval by CITY to any sublease hereof, TENANT shall agree to be primarily and jointly and severally liable to CITY for all obligations due CITY by any subtenant, including the payment of rents, and TENANT shall agree that CITY may proceed directly against TENANT for any obligation owing CITY by the subtenant. If this Lease is guaranteed, neither

the sublease nor CITY'S approval thereof shall release the guarantor from its obligations pursuant to the guaranty.

Section 10.09 Nondisturbance.

On the terms set forth below, CITY may enter into agreements with subtenants providing that in the event of any termination of this Lease prior to the expiration date, CITY will not terminate or otherwise disturb the rights of the subtenant under such sublease, but will instead honor such sublease as if such agreement had been entered into directly between Landlord and such subtenant, conditioned upon such subtenant's agreement to attorn to Landlord and full performance of all obligations under the sublease in question ("Non-Disturbance Agreement"). CITY agrees to execute a Non-Disturbance Agreement in connection with a particular sublease provided that Tenant provides CITY with a copy of the sublease, and the Non-Disturbance Agreement is customary in form and substance and otherwise reasonably acceptable to CITY.

Article 11 DEFAULT AND TERMINATION

Section 11.01 Abandonment by TENANT.

If TENANT breaches this Lease and abandons all or any part of the Premises prior to the scheduled expiration of the term of this Lease, CITY may continue this Lease in effect by not terminating TENANT'S right to possession of the Premises, in which event CITY shall be entitled to enforce all CITY'S rights and remedies under this Lease including the right to recover the Rent specified in this Lease as it becomes due under this Lease.

Section 11.02 Termination for Breach by TENANT.

All covenants and agreements contained in this Lease are declared to be conditions to this Lease and to the term hereby demised to TENANT. Should TENANT fail to perform any covenant, condition, or agreement contained in this Lease, except for payment of any Rent or other monetary amount due, and such failure is not cured within thirty (30) days after written notice thereof is served on TENANT, then CITY may terminate this Lease immediately, and in the event of such termination, TENANT shall have no further rights hereunder and TENANT shall thereupon forthwith remove from the Premises and shall have no further right or claim thereto and CITY shall immediately thereupon have the right to re-enter and take possession of the Premises, subject only to appropriate legal process.

Section 11.03 Termination for Failure to Pay Rent.

If any payment of Rent is not made as herein provided and such failure to pay is not cured within three (3) days after written notice thereof is served on the TENANT, CITY shall have the option to immediately terminate this Lease; and in the event of such termination, TENANT shall have no further right or claim thereto and CITY shall immediately thereupon have the right to re-enter and take possession of the Premises, subject only to appropriate legal process.

Section 11.04 Lender May Cure Default.

CITY shall afford the Lender under any Leasehold Encumbrance of record with CITY the right to cure any default by TENANT of the covenants, conditions, or agreements hereof, as provided in Article 5 of this Lease.

Section 11.05 Attorneys' Fees.

In the event the CITY finds it necessary to retain an attorney in connection with the default by the TENANT or enforcement of any of the terms, conditions, and covenants of this Lease, even though litigation is not instituted, TENANT shall pay to CITY its reasonable attorneys' fees. Non-payment of attorneys' fees by TENANT within three (3) days after written notice is served on TENANT shall give rise to an independent legal action by CITY to collect same. If CITY is successful in such legal action, CITY shall also be entitled to attorney fees and costs for the collection action. To the extent that CITY is represented by the City Attorney, a reasonable sum for such attorneys' services will be included as attorneys' fees.

Section 11.06 Damages for Breach.

If TENANT defaults in the performance of any covenant, condition or agreement contained in this Lease and the default be incurable or not be cured within the time period set forth hereinabove, then CITY may terminate this Lease and:

(1) Bring an action to recover from TENANT:

(a) The worth at the time of award of the unpaid rent which had been earned at the time of termination of this Lease;

(b) The worth at the time of award of the amount by which the unpaid rent which would have been earned after termination of this Lease until the time of award exceeds the amount of rental loss that TENANT proves could have been reasonably avoided;

(c) The worth at the time of award of the amount by which the unpaid rent for the balance of the term after the time of award exceeds the amount of rental loss that TENANT proves could be reasonably avoided; and

(d) Any other amount necessary to compensate CITY for all detriment proximately caused by TENANT'S failure to perform its obligations under this Lease; and

(2) Bring an action, in addition to or in lieu of the action described in subparagraph (1) of this Section, to re-enter and regain possession of the Premises in the manner provided by the laws of unlawful detainer of the State of California then in effect.

Section 11.07 Cumulative Remedies.

The remedies available to CITY in this Article shall not be exclusive but shall be cumulative with and in addition to all remedies now or hereafter allowed by law or elsewhere provided in this Lease.

Section 11.08 Waiver of Breach.

The waiver by CITY of any breach by TENANT of any of the provisions of this Lease shall not constitute a continuing waiver or a waiver of any subsequent breach by TENANT either of the same or a different provision of this Lease.

Section 11.09 Surrender of Premises.

On expiration or sooner termination of this Lease, TENANT shall surrender the Premises, and, subject to Section 4.04, all improvements in or on the Premises, and all facilities in any way appertaining to the Premises, to CITY in good, safe, and clean condition, reasonable wear and tear excepted.

Article 12 MISCELLANEOUS

Section 12.01 Attorneys' Fees.

If any litigation is commenced between the Parties concerning the Premises, this Lease, or the rights and duties of either in relation thereto, then the Party prevailing in such litigation shall be entitled, in addition to such other relief as may be granted in the litigation, to a reasonable sum as and for its attorneys' fees and court costs in such litigation, which shall be determined by the court in such litigation or in a separate action brought for that purpose. The "prevailing" party shall mean the Party who obtains substantially the relief sought by that Party.

Section 12.02 Notices.

Any and all notice or demands by or from CITY to TENANT, or TENANT to CITY, shall be in writing. They shall be served either personally, or by registered or certified mail. Any notice or demand to CITY may be given to:

City of Morro Bay
Attn: Harbor Director
1275 Embarcadero
Morro Bay, CA 93442

with a copy to:

City of Morro Bay
Attn: City Manager
City Hall
595 Harbor Street
Morro Bay, CA 93442

Any notice or demand to TENANT may be given at:

TLC Family Enterprises, Inc.
665 Kings Avenue
Morro Bay, CA 93442

Such addresses may be changed by written notice by either party to the other Party.

Section 12.03 Governing Law and Jurisdiction.

This Lease, and all matters relating to this Lease, shall be governed by the laws of the State of California in force at the time any need for interpretation of this Lease or any decision concerning this Lease arises. CITY and TENANT consent to exclusive personal and subject matter jurisdiction in the Superior Court of the State of California in and for the county where the Premises are located, and each Party waives any claim that such court is not a convenient forum. Each Party hereby specifically waives the provisions of California Code of Civil Procedure Section 394, and any successor statute thereto.

Section 12.04 Binding on Successors.

Subject to the provisions herein relating to assignment and subletting each and all of the terms, conditions, and agreements herein contained shall be binding upon and inure to the benefit of the successors and assigns of any and all of the Parties; and all of the Parties shall be jointly and severally liable hereunder.

Section 12.05 Partial Invalidity.

Should any provision of this Lease be held by a court of competent jurisdiction to be either invalid, void, or unenforceable, the remaining provisions of this Lease shall remain in full force and effect unimpaired by the holding.

Section 12.06 Sole and Only Agreement.

This Lease and the COL, including all exhibits incorporated by reference, constitutes the sole and only agreements between CITY and TENANT respecting the Premises and the leasing of the Premises to TENANT. Any other agreements or representations respecting the Premises and their leasing to TENANT by CITY, which are not expressly set forth in this Lease, are null and void. This lease terms herein specified correctly set forth the obligations of CITY and TENANT as of the date of this Lease. No modification, amendment, or alteration of this Lease shall be valid unless it is in writing and signed by the Parties.

Section 12.07 Modification.

This agreement shall not be modified except pursuant to a written agreement executed by the MAYOR and CITY CLERK pursuant to prior CITY Council approval. Notwithstanding CITY Council approval, no agreement shall become effective until such agreement is in fact executed by the MAYOR and CITY CLERK. TENANT understands that this agreement may not be modified by oral statements by any person representing the CITY including the MAYOR and CITY CLERK. TENANT specifically agrees not to rely on oral statements, purported oral waivers, or purported oral modifications and agrees not to rely upon purported written modifications unless they meet the requirements of this paragraph and are approved in writing pursuant to formal City Council action and a subsequent written modification signed by the MAYOR and CITY CLERK. If the title of any person authorized to act for CITY under this Lease shall be changed during the term of this Lease, then the person who succeeds to substantially the same responsibilities with respect to the CITY shall have the authority to act for CITY under this Lease.

Section 12.08 Time of Essence.

Time is expressly declared to be the essence of this Lease.

Section 12.09 Memorandum of Lease for Recording.

CITY and TENANT shall, at the request of either at any time during the term of this Lease, execute a memorandum or "short form" of this Lease, which shall describe the Parties, set

forth a description of the leased premises, specify the term of this Lease, and incorporate this Lease by reference.

Article 13 SPECIAL PROVISIONS PECULIAR TO THIS LEASE SITE

The following provisions apply to this Lease site only:

Section 13.01 TENANT'S Obligation to Redevelop Site

TENANT has proposed a major redevelopment project for the Premises (Proposed Redevelopment) and was granted the COL and the Parties intend this Lease to be an interim lease; (i) to allow TENANT to manage and operate the Premises and cause some use of the previous restaurant portion of the Premises and (ii) for the Parties an opportunity to negotiate a permanent lease for the Premises, all while TENANT is processing permits and completing design/development of the Proposed Redevelopment. TENANT agrees it shall be a material default and breach of this Lease if TENANT fails to meet the following time frames for the Proposed Redevelopment.

1. TENANT must obtain Concept Plan approval from the Planning Commission and City Council on or before August 31, 2018 at 4:00 p.m. or this Consent of Landowner Agreement will expire on September 1, 2018.
2. TENANT, after obtaining Concept Plan approval by the Planning Commission and City Council, shall negotiate in good faith with CITY for a new lease for the Premises. Upon execution of the new lease, the COL shall no longer be of any effect, and the new lease will replace this Lease. If a new lease is not executed by the Parties on or before October 25, 2018, then the COL shall expire on October 26, 2018; and, unless this Lease is extended by mutual agreement of the Parties, the provisions of Section 1.03 shall apply.

EXECUTED on ^{May 2}~~April~~, 2018, at Morro Bay, San Luis Obispo County, California.

CITY OF MORRO BAY

MAYOR *James L. Spaw*

TCL Family Enterprises, Inc., a California corporation

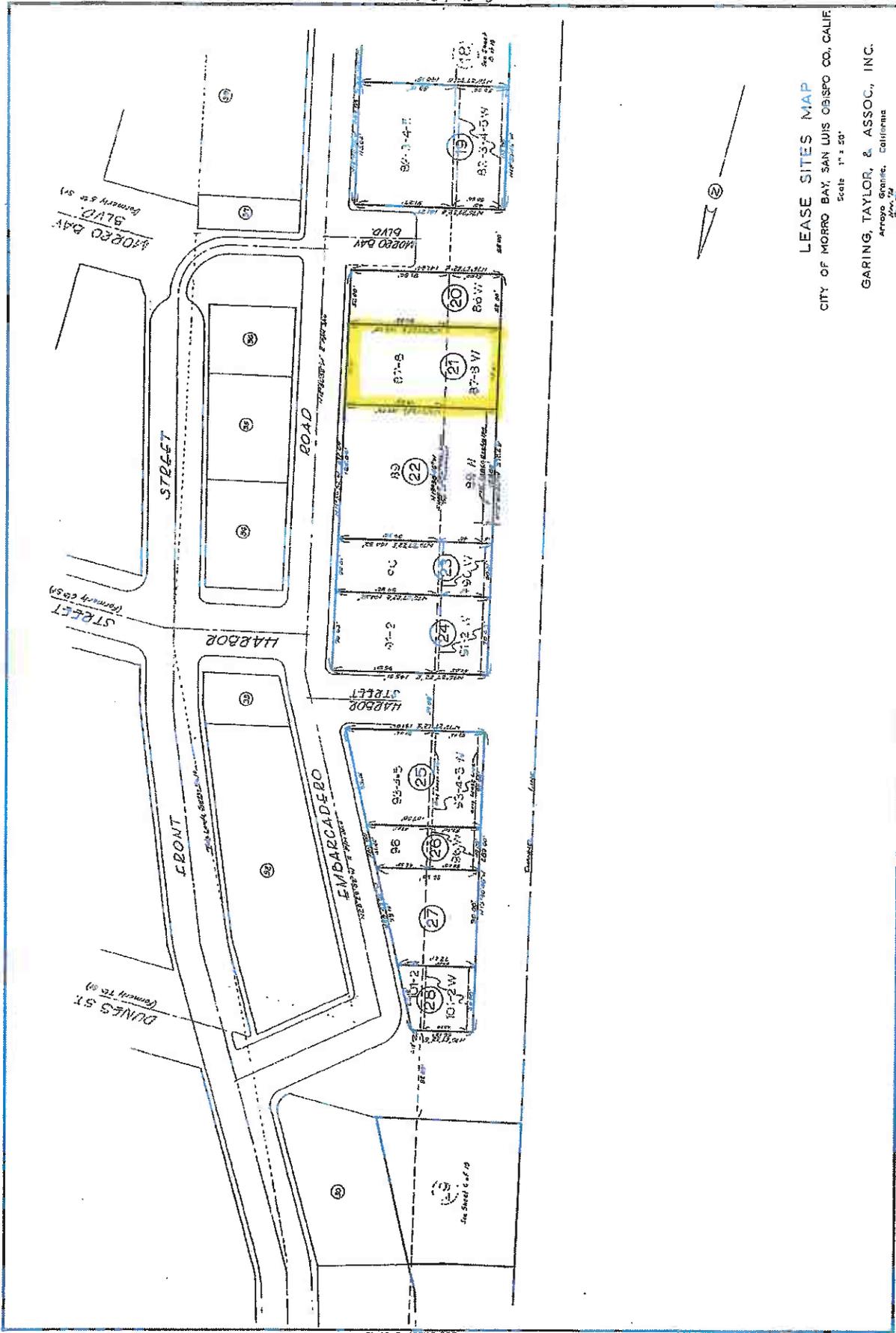
By: *[Signature]*

By: *[Signature]*

ATTEST:

Dane Swanson
CITY CLERK

EXHIBIT A
COPY OF PARCEL MAP



LEASE SITES MAP

CITY OF MORRO BAY, SAN LUIS OBISPO CO., CALIF.

Scale 1" = 50'

GARING, TAYLOR, & ASSOC., INC.

Atty. Gen. California

Sheet 7 of 13

EXHIBIT B

CITY OF MORRO BAY

595 Harbor St.
Morro Bay, CA 93442
(805) 772-6200
FAX (805) 772-7329

INSURANCE REQUIREMENTS FOR LESSEES (NO AUTO RISKS)

Lessee shall procure and maintain for the duration of the contract insurance against claims for injuries to persons or damages to property which may arise from or in connection with the Lessee's operation and use of the leased premises. The cost of such insurance shall be borne by the Lessee.

Minimum Scope of Insurance

Coverage shall be at least as broad as:

1. Insurance Services Office Commercial General Liability coverage (occurrence form CG 0001).
2. Workers' Compensation insurance as required by the State of California and Employer's Liability Insurance (for lessees with employees).
3. Property insurance against all risks of loss to any tenant improvements or betterments.

Minimum Limits of Insurance

Lessee shall maintain limits no less than:

1. General Liability: **\$1,000,000** per occurrence for bodily injury, personal injury and property damage. If Commercial General Liability Insurance or other form with a general aggregate limit is used, either the general aggregate limit shall apply separately to this project/location or the general aggregate limit shall be twice the required occurrence limit.
2. Employer's Liability: **\$1,000,000** per accident for bodily injury or disease.
3. Property Insurance: Full replacement cost with no coinsurance penalty provision.

City of Morro Bay
Insurance Requirements for Lessees

Deductibles and Self-Insured Retentions

Any deductibles or self-insured retentions must be declared to and approved by the City. At the option of the City, either: the insurer shall reduce or eliminate such deductibles or self-insured retentions as respects the City, its officers, officials, employees and volunteers; or the Lessee shall provide a financial guarantee satisfactory to the City guaranteeing payment of losses and related investigations, claim administration and defense expenses.

Other Insurance Provisions

The general liability policy is to contain, or be endorsed to contain, the following provisions:

1. The City, its officers, officials, employees, and volunteers are to be covered as insureds with respect to liability arising out of ownership, maintenance or use of that part of the premises leased to the Lessee.
2. The Lessee's insurance coverage shall be primary insurance as respects the City, its officers, officials, employees, and volunteers. Any insurance or self-insurance maintained by the City, its officers, officials, employees, or volunteers shall be excess of the Lessee's insurance and shall not contribute with it.
3. Each insurance policy required by this clause shall be endorsed to state that coverage shall not be canceled, except after thirty (30) days' prior written notice by certified mail, return receipt requested, has been given to the City.

Acceptability of Insurers

Insurance is to be placed with insurers with a current A.M. Best's rating of no less than A:VII.

Verification of Coverage

Lessee shall furnish the City with original certificates and amendatory **endorsements** effecting coverage required by this clause. The endorsements should be on forms provided by the City or on other than the City's forms, provided those endorsements or policies conform to the requirements. All certificates and endorsements are to be received and approved by the City **before** use of City premises. The City reserves the right to require complete, certified copies of all required insurance policies, including endorsements effecting the coverage required by these specifications at any time.

City of Morro Bay
Insurance Requirements for Lessees

Sub-lessee

Lessee shall include all sub-lessees as insureds under its policies or shall furnish separate certificates and endorsements for each sub-lessee. All coverages for sub-lessees shall be subject to all of the requirements stated herein.

Insurance\SpecC
Rev. 8/01

City of Morro Bay
Insurance Requirements for Lessees

Reproduction of Insurance Services Office, Inc. Form

INSURER: ISO Form CG 20 11 11 85 (Modified)
POLICY NUMBER: Commercial General Liability
ENDORSEMENT NUMBER:

THIS ENDORSEMENT CHANGES THE POLICY, PLEASE READ IT CAREFULLY.

ADDITIONAL INSURED -- MANAGERS OR LESSORS OF PREMISES

This endorsement modifies insurance provided under the following:
COMMERCIAL GENERAL LIABILITY COVERAGE PART.

SCHEDULE

1. Designation of Premises (Part Leased to You):
2. Name of Person or Organization (Additional Insured): City of Morro Bay
3. Additional Premium:

(If no entry appears above, the information required to complete this endorsement will be shown in the Declarations as applicable to this endorsement.)

WHO IS AN INSURED (Section II) is amended to include as an insured the person or organization shown in the Schedule, but only with respect to liability arising out of the ownership, maintenance or use of that part of the premises leased to you and shown in the Schedule and subject to the following additional exclusions:

This insurance does not apply to:

1. Any "occurrence" which takes place after you cease to be a tenant in that premises.
2. Structural alterations, new construction or demolition operations performed by or on behalf of the person or organization shown in the schedule.

Modifications to ISO form CG 20 11 11 85:

1. The Insured scheduled above includes the Insured's elected or appointed officers, officials, employees and volunteers.
2. This insurance shall be primary as respects the Insured shown in the schedule above, or if excess, shall stand in an unbroken chain of coverage excess of the Named Insured's scheduled underlying primary coverage. In either event, any other insurance maintained by the Insured scheduled above shall be in excess of this insurance and shall not be called upon to contribute with it.
3. The insurance afforded by this policy shall not be canceled except after thirty days prior written notice by certified mail return receipt requested has been given to the City.

Signature-Authorized Representative

Address

CG 20 11 11 85 Insurance Services Office, Inc. Form (Modified)
Insurance\Form#3
Rev. 8/01

01181.0024/466264.5 JWP
Spec C

RESOLUTION NO. 98-18

**RESOLUTION OF THE CITY COUNCIL
OF THE CITY OF MORRO BAY, CALIFORNIA
APPROVING A 50-YEAR MASTER LEASE AGREEMENT FOR
LEASE SITE 87-88/87W-88W BETWEEN THE CITY OF MORRO BAY
AND TLC FAMILY ENTERPRISES, LOCATED AT 833 EMBARCADERO**

**THE CITY COUNCIL
City of Morro Bay, California**

WHEREAS, the City of Morro Bay is the lessor of certain properties on the Morro Bay Waterfront described as City Tidelands leases and properties; and

WHEREAS, TLC Family Enterprises (Travis Leage and Cherise Hansson) has been the interim lessee of Lease Site 87-88/87W-88W since April 2018 and is a tenant in good standing; and

WHEREAS, TLC Family Enterprises was granted Consent of Landowner approval for a proposed complete lease site redevelopment project consisting of a new building with retail, hotel, restaurant, and bar uses, outside children's play area, new slips/docks and public access improvements including the HarborWalk; and

WHEREAS, TLC Family Enterprises has obtained Concept Plan approval from the Planning Commission and City Council for their proposed redevelopment project; and

WHEREAS, in accordance with the City's Master Lease Policy, the City and lessee have agreed to a new 50-year lease agreement for Lease Site 87-88/87W-88W located at 833 Embarcadero.

NOW, THEREFORE, BE IT RESOLVED by the City Council of the City of Morro Bay, California, as follows:

1. The attached new Master Lease Agreement for Lease Site 87-88/87W-88W is hereby approved.
2. The Mayor is hereby authorized to execute said Master Lease Agreement.

PASSED AND ADOPTED by the City Council of the City of Morro Bay at a special meeting thereof held on the 11th day of December 2018 on the following vote:

AYES:
NOES:
ABSENT:

JAMIE L. IRONS, Mayor

ATTEST:

DANA SWANSON, City Clerk