



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Jon Cicirelli

SUBJECT: SEE BELOW

DATE: February 5, 2024

Approved

Date

2/13/24

COUNCIL DISTRICT: 8

SUBJECT: RAGING WATERS LEASE ASSIGNMENT, AMENDMENT, AND LONG-TERM REQUEST FOR PROPOSAL DEVELOPMENT

RECOMMENDATION

- (a) Adopt a resolution authorizing the City Manager or her designee, to:
- i. Negotiate and execute an assignment, and all other necessary and/or ancillary documents, of the ground lease dated March 5, 1985, between the City of San José and Thomas J. Lochtefeld (present assignee Palace Entertainment), to California Dreamin' Entertainment, Inc., as new assignee, for the Raging Waters water park located at Lake Cunningham; and
 - ii. Negotiate and execute an amendment to the ground lease between the City of San José and California Dreamin' Entertainment, Inc., extending the lease for six months with an option to extend for an additional six months at the City's sole discretion, increasing lessee's payments to the City to six percent of all gross receipts, and reimbursing lessee for up to \$3,450,000 for capital and facility repairs and initial operating costs for the Raging Waters water park, subject to City Council appropriation.
- (b) Provide feedback to staff on proposed Guiding Principles for a Request for Proposal for a long-term operator of Lake Cunningham Regional Park attractions, including the operation of the Raging Waters water theme park.

SUMMARY AND OUTCOME

This action will result in the assignment of an amendment to the lease for the operation of Raging Waters so the facility can be operated and maintained while staff conducts a Request for Proposal (RFP) for long-term operations of the water park and potentially other areas in Lake Cunningham Regional Park. With approval of this recommendation, the assignee, California

Dreamin' Entertainment, Inc., (Assignee) will be able to begin making repairs and preparations to open the park for the 2024 summer season so that residents and visitors will be able to enjoy Raging Waters, the facility will be maintained, recreational and economic activity will be generated, and the Assignee will pay rent to the City.

BACKGROUND

The City of San José's Lake Cunningham Regional Park in East San José includes Raging Waters, a water theme park. The facility is owned by the City of San José and is currently comprised of 14 water rides and attractions, cabanas, concessions, a gift shop, and amphitheater event space. Raging Waters, located on City parkland, is one of the marquee destinations in the large inventory of parks, trails, and recreational facilities that the Department of Parks, Recreation, and Neighborhood Services (PRNS) oversees.

Raging Waters had its start in the early 1980s. The following is a brief timeline of events related to its development and lease agreements.

- In June 1983, the City Council approved the revised master plan for Lake Cunningham Regional Park, which incorporated the concept of a water theme park.
- In March 1985, the City Council approved a 20-year ground lease between the City and Raging Waters for the development and operation of a 23-acre water theme park at the site, which opened to the public in the summer of 1985 as the largest water park in Northern California.
- In September 1994, the City Council approved a lease amendment to provide for Raging Waters' construction of additional capital improvements and to revise lease terms.
- In March 1995, the City Council approved a fourth amendment that extended the lease by 20 years, from March 5, 2005 to March 5, 2025, approved the construction of additional improvements, revised the rent schedule, and established a capital improvement fund.
- In May 1995, the City Council approved the assignment and assumption of the lease from Raging Waters to Paramount Parks, Inc.
- In April 2011, the City entered into a sixth restated lease amendment where Paramount Parks, Inc. changed its name to Palace Entertainment and the contribution to lessee's maintenance obligation was modified.
- On September 5, 2023, Palace Entertainment notified City staff that it intended to terminate the agreement on September 30, 2023. The current lease expires on March 5, 2025.

With its actions, Palace Entertainment is in breach of the agreement in the following areas:

- Abandonment of the lease premises by lessee (Lease Agreement Section 17.02);
- Failure to operate lease premises for public outdoor recreation purposes (Lease Agreement Section 1.02);
- Failure to make rental payments to the City (Lease Agreement Section 17.02);

- Failure to provide onsite security at lease premises (Lease Agreement Section 10.01); and
- Failure to keep and maintain leased premises in good order, condition, and repair (Lease Agreement Section 4.03).

Staff has since been in communication with Palace Entertainment regarding its lease obligations.

As Palace Entertainment vacated the premises, PRNS and the Department of Public Works assessed the condition of the facility, identified deferred maintenance that had impacted the overall condition of the park, and noted some equipment needed to operate the facility had been removed. Current conditions can worsen without daily maintenance and, for operations to resume, critical repairs must be addressed at significant cost. Additionally, some previously identified deficiencies were not addressed by Palace Entertainment and repairs are now substantial projects with great costs. For example, well in advance of Palace Entertainment vacating the premises, staff inquired about a ride that had been inoperable for a few years. Initially, staff was told that Palace Entertainment was working with the manufacturer and other companies to make needed repairs. In the past year, staff learned that the manufacturer and other companies declined to make repairs and Palace Entertainment staff reported it had plans to replace the slide with a new attraction. The slide was not replaced and remains inoperable.

After Palace Entertainment announced the closure of Raging Waters, six companies contacted PRNS with interest in operating the water park. The existing lease stipulates that, with City Manager approval, the City can assign the current lease agreement to a proposed assignee that meets the following qualifications outlined in the lease agreement:

- Is an experienced, successful, and reputable developer and constructor of major water theme parks, if the assignment or sublease is during any construction phase;
- Is an experienced, successful, and reputable operator of major water theme parks;
- Has a net worth exceeding \$6,000,000;
- Is in sufficient financial condition to handle the lease obligations with adequate security to the City, including furnishing the City with a performance bond required under the lease; and
- Has an excellent reputation for business operations and service to the public.

Prior to Palace Entertainment's announcement, staff had already begun to prepare a process to solicit new ideas and programs for the facility, as the current contract was approaching the March 5, 2025 lease end date. Upon receiving substantial interest from parties seeking to assume operations and to protect the City's substantial assets by securing continued maintenance, staff moved quickly to develop and administer a process to select an assignee to assume operations and maintenance of Raging Waters, to keep this popular destination available to the community and to attract visitors to Lake Cunningham Regional Park in East San José.

ANALYSIS

Lease Assignment Process and Selection

Staff implemented a structured process to select an assignee within an abbreviated timeline. On October 20, 2023, staff issued a letter to all parties that had expressed an interest in operating Raging Waters to PRNS staff, offering an opportunity to submit qualifications to be considered for an assignment of the existing lease. Responses outlining how each company met the required qualifications were due by October 27, 2023. Five organizations submitted documents with their qualifications. Staff from PRNS and the Office of Economic Development and Cultural Affairs reviewed response submissions on October 30, 2023 and determined that four of the five submissions demonstrated meeting required qualifications.

Staff invited companies meeting required qualifications to tour the facility on November 8, 2023 and provided them with proposal submission guidelines and a questionnaire that was due on November 17, 2023. Staff asked proposers to provide a business plan, including financial viability, management/operations plan, marketing plan, and proposed timeline for reopening.

Three organizations submitted proposals, one of which was only interested in a long-term lease. Staff from PRNS and Office of Economic Development and Cultural Affairs reviewed the remaining two proposals using the following criteria: viability of proposal concept, business experience, financial resources, operational proposal, and operating standards. Both proposals included requirements to secure their up-front investments if they were not selected to be the long-term operators of the facility during the RFP process that staff will conduct this year. Both proposers were invited to interview. Staff interviewed the finalists on December 8, 2023, asking questions to further evaluate the two proposals. The highest rated assignee candidate, based on these interviews, asked for and was granted an opportunity to conduct an additional assessment of conditions at Raging Waters and proposed a detailed and itemized plan to reestablish operations, including the equipment purchase and facility repairs needed to reopen the park detailed below.

The Assignee as selected for the Raging Waters lease assignment. The Assignee was founded in 2023 by theme park executives who were recently awarded the lease to redevelop the former Raging Waters in Sacramento, California at Cal Expo. On average, each team member has over 40 years of experience in the industry. Like the case with the City, Palace Entertainment terminated its lease with the State of California and left that park, too. In Sacramento, the Assignee was selected over five other bidders and has negotiated a comprehensive lease with the State of California.

The Assignee's proposal for Raging Waters includes incorporating temporary structures and food trucks to mitigate the short timeline for reopening for summer 2024 and ensure customers continue to receive quality services. Additionally, the Assignee secured partnerships with Chuck E. Cheese and reputable food truck companies that it plans to utilize during the short-term lease. The proposal also includes plans to open a wine garden to attract new users and expand operations beyond the summer and traditional operating hours. The Assignee proposed an

increased rent payment of six percent of sales to the City (the current contract is 5.5 percent) and projected gross revenues of \$6,418,000 in the first year.

Lease Amendment Terms

The Assignee and City will negotiate and execute an assignment and assumption agreement of the Palace Entertainment lease with the same terms and conditions, however, based on the Assignee's proposal, the following terms are recommended to be amended in the assigned lease:

Term	Description																								
Lease Term Extension	Extend the lease term for six months, from March 5, 2025 to September 5, 2025, with an option to extend for an additional six months at the City's sole discretion.																								
Payments to City	Six percent of all gross receipts to the City. The current contract is 5.5 percent.																								
Costs to Resume Operations	<p>Assignee estimated that up to \$4,372,000 will be spent to resume operations, including making repairs, buying equipment and inventories, hiring personnel, and preparing for reopening. Estimated reopening expenses are summarized below.</p> <table> <tr> <td colspan="2">Estimated Reopening Expenses:</td></tr> <tr> <td>Capital repairs</td><td>\$695,000</td></tr> <tr> <td>Fixtures, furnishings, and equipment</td><td>\$613,000</td></tr> <tr> <td>Pre-opening personnel and training</td><td>\$562,000</td></tr> <tr> <td>Borrowing costs (interest expense)</td><td>\$462,000</td></tr> <tr> <td>Contingencies for capital project, facility repair, and other costs</td><td>\$413,000</td></tr> <tr> <td>Facilities repairs</td><td>\$377,000</td></tr> <tr> <td>Landscaping</td><td>\$280,000</td></tr> <tr> <td>Initial inventories</td><td>\$215,000</td></tr> <tr> <td>Licenses</td><td>\$135,000</td></tr> <tr> <td>Other (taxes, marketing, insurance, etc.)</td><td>\$620,000</td></tr> <tr> <td>Total</td><td>\$4,372,000</td></tr> </table> <p>The Assignee will pay for these reopening expenses. Of this amount, the Assignee estimated that \$922,000 may be recovered by selling transferrable assets, primarily fixtures, furnishings, equipment and inventories, to a successor if it is not selected for the long-term operation through the RFP. In the event that it is not selected for the long-term operation, the Assignee seeks reimbursement of the remaining capital and start-up costs, up to \$3,450,000, with all expenses subject to City staff approval. The future RFP for long-term operations will include a requirement for the selected operator to reimburse the Assignee up to \$3,450,000, if the Assignee is not the ongoing vendor selected from the RFP process.</p>	Estimated Reopening Expenses:		Capital repairs	\$695,000	Fixtures, furnishings, and equipment	\$613,000	Pre-opening personnel and training	\$562,000	Borrowing costs (interest expense)	\$462,000	Contingencies for capital project, facility repair, and other costs	\$413,000	Facilities repairs	\$377,000	Landscaping	\$280,000	Initial inventories	\$215,000	Licenses	\$135,000	Other (taxes, marketing, insurance, etc.)	\$620,000	Total	\$4,372,000
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Guiding Principles for Raging Waters and Lake Cunningham Long-Term Operation RFP

In March 2023, two years before the expiration of the 40-year lease for Raging Waters, staff began researching and planning for the RFP to select a long-term operator for the water park. Now, in parallel to the assignment of the Raging Waters lease to a short-term operator, PRNS and Office of Economic Development and Cultural Affairs staff have begun drafting an RFP for a long-term operator that can provide sustainable growth opportunities for Raging Waters and potentially other areas of Lake Cunningham Regional Park, such as the marina. Although Section 1700 of the City Charter generally does not allow long-term agreements on parkland, voters approved Measure M on November 6, 1990 that allowed portions of Lake Cunningham Regional Park to be leased for a term not to exceed 55 years and restricted revenues from such leases to public park and recreation purposes. The City's selection of a long-term operator in the upcoming RFP process falls under that authority.

As staff has begun drafting the scope of the RFP, staff has centered the Guiding Principles of ActivateSJ, the 20-year strategic plan for PRNS, in the RFP's goals. City Council and community feedback is welcomed on the following goals that will become the basis for further development of this complex and impactful RFP.

- **Stewardship:** Capital investment into Raging Waters and potentially other areas of Lake Cunningham Regional Park and operations and maintenance of those amenities at the expense and risk of the company or companies selected to operate, along with lease revenue to the City that can support park infrastructure and maintenance.
- **Nature:** A contribution towards solving the water quality challenge at Lake Cunningham and creating conditions that could allow for future lake sports and recreation.
- **Equity and Access and Public Life:** A safe, affordable, customer-friendly, and high-quality water theme park experience for San José residents that encourages healthy outdoor recreational activity, socialization, and community engagement while also retaining public park access and amenities at Lake Cunningham.
- **Identity:** A destination that draws residents and visitors from across the region to support the local economy and raises the profile of San José overall and specifically East San José neighborhoods around Lake Cunningham.

The RFP is scheduled to be released by spring 2024 and evaluated through the summer. Staff expects to return to the City Council in late 2024 or early 2025 to award the RFP and to transition to a new operator in 2025 after negotiating and executing lease agreements.

EVALUATION AND FOLLOW-UP

Once the RFP is concluded, staff will return to the City Council with the outcome of the bid process and recommended award. Lease negotiations will then commence with a goal of transitioning operators, if necessary, in 2025.

For the current lease assignment and assumption, the Assignee will accept all terms and conditions of the existing lease agreement subject to the amendments outlined in this

memorandum. The lease agreement requires the lessee to meet monthly with City staff to review operational performance and revenue. Additionally, the lessee is required to submit monthly revenue reports, an annual financial audit, and all state safety inspection reports to ensure all attractions are maintained and safe for operations. Staff will continue to monitor for compliance and hold the Assignee accountable to these terms.

COST SUMMARY/IMPLICATIONS

The Assignee will make lease payments of six percent of gross receipts to the City during the assignment, which staff conservatively estimates to be \$250,000 for the 2024 season that straddles the end of Fiscal Year 2023-2024 and early months of Fiscal Year 2024-2025. Lease payments may amount to \$350,000 if the Assignee achieves its forecasted gross receipts. Additionally, the resumption of Raging Waters operations in summer 2024 will result in approximately \$47,500 in parking fees at Lake Cunningham. Both the lease payments and parking revenues will be deposited in the Lake Cunningham Fund that can support Lake Cunningham Regional Park operations, maintenance, and improvements. In addition, assigning the lease with recommended amendments will also ensure the water theme park is secured and maintained until a long-term operator is identified through the upcoming RFP, relieving the City of further expenses for these needs that have already amounted to approximately \$100,000 in contract security and irrigation repairs as of the time of writing of this memorandum.

The Assignee will pay for the reopening expenses of \$4,372,000. Of this amount, the Assignee estimated that \$922,000 may be recovered by selling transferrable assets, primarily fixtures, furnishings, equipment, and inventories to a successor if it is not selected for the long-term operation through the RFP. If it is not selected for the long-term operation, the Assignee seeks reimbursement of the remaining capital and start-up costs, up to \$3,450,000, with all expenses subject to City staff approval. The future RFP for long-term operations will include a requirement for the selected operator to reimburse the Assignee up to \$3,450,000 from the selected operator's own funds, if the Assignee is not the ongoing vendor selected from the RFP process.

COORDINATION

This memorandum was coordinated with the City Attorney's Office, City Manager's Budget Office, and City Manager's Office of Economic Development and Cultural Affairs.

PUBLIC OUTREACH

This memorandum will be posted on the City's Council Agenda website for the February 27, 2024 City Council meeting.

HONORABLE MAYOR AND CITY COUNCIL

February 5, 2024

Subject: Raging Waters Lease Assignment, Amendment, and Long-Term Request for Proposal Development

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COMMISSION RECOMMENDATION AND INPUT

No commission recommendation or input is associated with this action.

CEQA

Not a Project, File No. PP17-003, Agreements/Contracts (New or Amended) resulting in no physical changes to the environment.

PUBLIC SUBSIDY REPORTING

This item does not include a public subsidy as defined in section 53083 or 53083.1 of the California Government Code or the City's Open Government Resolution.

/s/

Jon Cicirelli
Director of Parks, Recreation
and Neighborhood Services

The principal authors of this memorandum are Shannon Heimer, Division Manager, and Dominique Pacolba, Parks Manager. For questions, please contact Avi Yotam, Deputy Director, at avi.yotam@sanjoseca.gov.