



# LEASING POLICY

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*This Port of Los Angeles Leasing Policy was prepared by the Harbor Department's Business Development Bureau and Real Estate Division in conjunction with IMC Municipal Consulting.*

TRANSMITTAL 1

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## **PORT MANAGEMENT**

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## SOURCES OF INFORMATION

Development of the Leasing Policy included information drawn from discussions with Port of Los Angeles staff, consulting firms, various port agencies located in the United States, and Port of Los Angeles tenants' and stakeholder feedback. The development process also included review of documentation from agencies which govern the operation of the Port of Los Angeles, professional real estate organizations, leasing policies from other ports located in the United States and familiarization with other Port of Los Angeles policies. Outreach and information sources are listed below.

- AIR Commercial Real Estate Association
- Building Owners and Managers Association International (BOMA)
- California State Lands Commission – Public Trust Doctrine
- City of Los Angeles Harbor Department Business Development Bureau and Real Estate Division
- City of Los Angeles Harbor Department, Office of the City Attorney
- City of Los Angeles Harbor Department Port Police
- IMC Consulting
- Los Angeles World Airports (LAWA)
- Los Angeles City Charter
- Los Angeles City Administrative Code
- Performance Audit of the Port of Los Angeles Real Estate Division (performed by Harvey M. Rose Associates, LLC)
- Port Everglades, Broward County, Florida
- Port of Long Beach, California
- Port of Los Angeles, 2012-2017 Strategic Plan
- Port of New York and New Jersey
- Port of Oakland, California
- Port of Portland, Oregon
- Port of San Diego, California
- Port of Vancouver, Washington
- State Tidelands Trust Grant
- Tubert Consulting

## INTRODUCTION

The Harbor Department is a proprietary department of the City of Los Angeles, more commonly known as the Port of Los Angeles (“Port”) and operates for the purpose of the promotion and accommodation of maritime commerce, navigation and fishery. As a proprietary department of the City of Los Angeles (“City”), the Port is financially independent of the City and self-sustaining. The Port is one of the State of California’s primary economic resources and an essential element of the national maritime industry.

The Port is primarily governed by the Los Angeles City Administrative Code (“Administrative Code”); Los Angeles City Charter (“City Charter”); the California Coastal Act-Chapter 8 (“Coastal Act”); the California State Lands Commission - Public Trust Doctrine (“Public Trust Doctrine”); Tariff No. 4, as it now exists or may be amended or superseded in the future, (“Tariff”); and the State Tidelands Trust Grant (“Tidelands Trust”). Management and control of the Port is directed by a five-member Board of Harbor Commissioners (“Board”) and administered by the Executive Director of the City of Los Angeles Harbor Department (“Executive Director”).

The Port oversees nearly 300 property agreements throughout the Harbor District which include concession agreements, leases, operating agreements, orders, permits, revocable permits, temporary entry and use permits, and other agreements. The Board adopted the current policy and procedures document February 1, 2006. Since that time the following has occurred:

- A “Performance Audit of the Port of Los Angeles Real Estate Division” (“Performance Audit”) was conducted in 2011;
- The Port of Los Angeles 2012-2017 Strategic Plan (“Strategic Plan”) was published in May 2012; and
- In May 2012, the Real Estate Division was re-organized to direct the focus of operations toward property management to better support the Port’s needs.

This Port of Los Angeles Leasing Policy (“Leasing Policy”) is separate from lease administrative and compliance procedures which address internal processes and procedures.

The Leasing Policy supports the Strategic Plan while reinforcing consistency with other Board approved policies, the Administrative Code, City Charter, Coastal Act, Public Trust Doctrine, Tariff, and the Tidelands Trust.

The Leasing Policy applies to all property agreements involving use and occupancy of land, submerged land, buildings, and other improvements although certain aspects may not apply to all forms of Agreement or in all circumstances (i.e. certain rules governing Operating Agreements). Further, this Leasing Policy does not replace or supplant City Charter or Administrative Code or other governing documents that apply to City functions. Rather, it provides a framework for the Port's internal use in making leasing decisions, increasing efficiency, and achieving consistency and transparency, as it relates to the following:

- a) Development of new property use agreements; and,
- b) Modifications to existing property use agreements, including compensation adjustments and resets.

The Leasing Policy affirms the Port's responsibilities as a custodian of Tidelands Trust properties and as a proprietary department including, but not limited to, the following obligations.

- Operation of the Port as a proprietary department independent of financial support from the City;
- Compliance with Board-approved policies, the California Coastal Act, and other federal, state and local laws, rules and regulations and applicable mandates; and,
- Maximization of Tidelands Trust property to achieve the highest and best use of the assets consistent with the Port's strategic goals and objectives.

The Leasing Policy upholds the Strategic Plan through alignment with its 3 key results areas – Competitive Operations, Strong Relationships, and Financial Strength. The key result areas are defined below.

- Competitive Operations. Development and maintenance of world-class infrastructure; retention and growth of market share; advance technology and sustainability; and/or optimization of land use.
- Strong Relationships. Creation of a positive work place culture and/or increase stakeholder, and community awareness and support.
- Financial Strength. Activity which strengthens the Port's financial performance.

The objectives of the Real Estate Policies and Procedures are to provide the following:

1. Specific guidelines for selecting Qualified Customers to enter into leases for available property;
2. An approval process that is consistent with the Board of Harbor Commissioners and the City of Los Angeles applicable policies and procedures;
3. Fair and equitable methods for potential and existing customers to conduct business with the Port;
4. Recognize existing relationships with current customers and their investment in the occupied terminal and premises;
5. Ensure that no one entity secures a competitive advantage by means of controlling a undue amount of Port property or berthing area;
6. A process for assembling, sharing, and maintaining information related to the proposed selection and negotiation processes in an open and transparent manner;
7. Optimizing of Tidelands Trust assets consistent with requirements of the State of California;
8. Use of available property consistent with the Port's Master Plan and strategic objectives;
9. Mutually agreeable provisions to prevent and control pollution to the extent feasible;
10. Achieve goals for local job participation and living wage requirements; and,
11. Periodically evaluate performance of leases.

The above objectives are reflected in the previously Board-adopted leasing policy and have been incorporated into this new Leasing Policy as well as a new Strategic Asset Management Policy ("Asset Management Policy").

## LEASING POLICY

### I. General Provisions

1. It is the policy of the Board that authority to implement this Leasing Policy is hereby delegated to the Executive Director.
2. It is the policy of the Board that the Leasing Policy shall apply to every type of Port property-use agreement to the extent applicable under law.
  - a. Leasing Policy Section III – Tenant in Good Standing, Section V – Term Options, Section VIII – Rates, Fees and Charges and Section IX – Compensation Adjustments do not apply to Operating Agreements. All other Leasing Policy sections may apply as appropriate.
3. It is the policy of the Board that all Lease Agreements shall be developed in complete accordance with, and governed by, the Leasing Policy.
4. It is the policy of the Board that the term “Tenant” shall apply to all parties that have or are being considered for a Lease Agreement with the Port.
5. It is the policy of the Board that the Leasing Policy shall remain in full force and effect unless and until changes are made by Board action.
6. It is the policy of the Board to review and update the Leasing Policy no less frequently than every five years following its adoption.
7. It is the policy of the Board that the Leasing Policy and the use of Port property shall be in agreement with the Administrative Code, City Charter, Coastal Act, Public Trust Doctrine, Tariff, and the Tidelands Trust, including giving priority to water-dependent uses that serve the maritime industry and optimize such property to its highest and best use consistent with the Port’s strategic goals and objectives.
8. It is the policy of the Board that the Leasing Policy shall not override or supersede the terms and conditions of any existing Lease Agreement or Tariff item, which defines rates, charges, rules and regulations, between the Port and a Tenant.
9. It is the policy of the Board that every Tenant shall adhere to all applicable and duly authorized policies of the Port and the City.
10. It is the policy of the Board that every Lease Agreement shall contain a provision for every Tenant to achieve goals of local job participation and living wage requirements as defined in the City of Los Angeles Administrative Code Section 10.37.

11. It is the policy of the Board that the Executive Director may execute a Lease Agreement on an “as-is, where-is, with all faults and limitations” basis. In such case, the Tenant shall be provided an opportunity to conduct due-diligence which may include a feasibility analysis and an environmental evaluation and inspection of the property to ascertain its condition. Such action shall be at Tenant’s sole expense.
12. It is the policy of the Board that all Port Tenant operations and uses shall adhere to all applicable building and fire codes and environmental standards including, but not limited to, federal, state, and local laws and regulations.
13. It is the policy of the Board that all Port Tenants shall provide for a safe environment and follow the Port’s Homeland Security rules and regulations, including, but not limited to, Tariff Section 2, item 298 and all other applicable federal, state and local policies and mandates.
14. It is the policy of the Board that use of all Port property shall be consistent with the Port’s Master Plan and all other land-use plans that establish future development of the Port.
15. It is the policy of the Board to require compensation for all Lease Agreements. Any exceptions must be approved by the Board, with findings, in an open public meeting.
16. It is the policy of the Board that all rates, fees and charges in the Leasing Policy shall be consistent with the Administrative Code, City Charter and all other applicable laws and regulations.
17. It is the policy of the Board that the use of Port property must allow for the key principle of the Public Trust Doctrine to include the promotion of public uses, (i.e. marinas, visitor serving retail), rather than exclusively private purposes.

## **II. Competitive Proposals**

1. It is the policy of the Board to solicit competitive proposals for available properties, including land and submerged land areas. It is also the policy of the Board to continue to build long-term relationships with existing Tenants. Therefore, the Board recognizes certain exceptions as set forth below.
  - a. The Executive Director shall have the discretion to enter into temporary entry and use permits, internal temporary entry and use permits, space assignments and certain 30-day revocable permits without a competitive proposal process.
  - b. The Executive Director shall have discretion to negotiate with an existing Tenant in Good Standing (as defined below in Section III) when the term

of the Lease Agreement expires rather than soliciting proposals for the leasehold.

- c. The Executive Director may enter into a Lease Agreement with a Tenant when land adjacent to that Tenant's existing leasehold becomes vacant and the productivity or efficiency of the existing Tenant can be enhanced by this property rather than soliciting competitive proposals.
2. It is the policy of the Board that all competitive proposals, and any exceptions to competitive processes, shall remain consistent with the Administrative Code, City Charter and all other applicable regulations.

### **III. Tenant in Good Standing**

1. It is the policy of the Board that a Tenant in good standing shall be determined by the ability to meet minimum qualifying standards with respect to the criteria set forth below, ("Tenant in Good Standing"). Such determination will be made by the Chief Financial Officer of the Port, who must attest to such determination in writing, and made part of the staff report and recommendation to the Board.
  - a. A Tenant in Good Standing shall be, at all times, in compliance with all terms and conditions of its Lease Agreement with the Port, including current in all payments due and owing under the Lease.
  - b. A Tenant in Good Standing shall demonstrate financial capability and responsibility.
  - c. A Tenant in Good Standing shall possess management qualifications and experience which meet industry standards.
  - d. A Tenant in Good Standing shall operate and use the property in the manner contemplated in the Lease.
  - e. The Board may use other applicable factors to assess the status of the Tenant.

#### **IV. Tenant Selection**

1. It is the policy of the Board to ensure that no one entity secures an unfair competitive advantage by controlling an undue amount of Port property or berthing area.
2. It is the policy of the Board that the manner of assembling, sharing, and maintaining information related to proposal selection and negotiation processes shall be performed in an open and transparent manner.
3. It is the policy of the Board that the Executive Director shall exercise due diligence when considering a new or renewal Lease Agreement. The due diligence process shall determine prospective and existing Tenants' abilities to comply with Lease Agreement terms and conditions. Such due diligence shall include, but is not limited to, the evaluation processes set forth below.
  - a. Appropriate analyses shall be conducted to determine Tenant qualifications and ability to comply with terms and conditions of the Lease Agreement.
  - b. Appropriate analyses shall be conducted regarding provisions of the above Section III, Tenant in Good Standing, to assess Tenant's status.
  - c. Appropriate vetting shall be conducted to determine Tenant performance against industry ratios and standards. A Tenant which meets certain ratios and standards shall be deemed a qualified user ("Qualified User").

#### **V. Term Options**

1. It is the policy of the Board that the option to extend the term of a Lease Agreement may be negotiated during the original lease transaction. However, in no event can the sum of the initial term, plus option period(s), exceed the maximum allowable term per the City Charter and Tidelands Trust.
2. It is the policy of the Board that in consideration of granting an option to extend the initial term, and/or subsequent term, of a Lease Agreement, certain conditions may apply as set forth below.
  - a. Tenant shall satisfy specified metrics and industry standards.
  - b. Tenant shall pay a fee that is, at minimum, 10% of the estimated annual base rent of the first year of said option period ("Option Fee"). Such Option Fee shall apply to each option period and shall be paid upon the execution of the initial term of the Lease Agreement.

- c. The Option Fee shall not apply to, but is in addition to, future rent and shall not be refundable.
- d. The Option Fee shall be fully refundable in the event the Port terminates the Lease Agreement for convenience of the Port's interest.

## **VI. Amendments**

1. It is the policy of the Board that the Executive Director may consider a material amendment to a Lease Agreement subject to some, or all, of the conditions set forth below.
  - a. Substantial capital investment in tenant improvements have been made by Tenant, as approved by the Port, or Tenant has maintained the premises in accordance with Port policies, particularly maintenance standards and environmental policies.
  - b. Qualification for an amendment shall require Tenant to be a Tenant in Good Standing.
  - c. Any use proposed by the amendment is consistent with applicable land-use plans.
  - d. All parts of the amended leasehold shall be developed or used for the permitted use and Tenant shall pay the newly determined fair market rent.
2. It is the policy of the Board, to have the discretion to prescribe other conditions when considering an amendment.

## **VII. Assignments and Subleases**

1. It is the policy of the Board that the Executive Director shall have no obligation to approve an assignment or consent to a sublease if the proposed transaction is not specifically contemplated and authorized in the provisions of the Lease Agreement. It is also the policy of the Board that certain requirements shall apply to assignments and subleasing as set forth below. Further, any consideration of an assignment may require a rent guarantee from the assignor and shall, at minimum, meet the conditions set forth below.
  - a. Assignee shall meet conditions of Qualified Users, as defined in the above Section IV, Tenant Selection, item 4.b., and other applicable qualifying standards.
  - b. An assignment shall not release the Tenant from its obligation under the Lease Agreement.

- c. Tenant shall not voluntarily or by operation of law assign, transfer, mortgage or encumber (collectively, “assign or assignment”) or sublet all or any part of Tenant’s leasehold interest without prior written consent of the Executive Director.
  - d. Change in Tenant’s ownership or assets may be considered an assignment and shall be subject to compliance with conditions of Qualified Users, as defined in the above Section IV, Tenant Selection, and require prior written consent of the Executive Director. Such change includes, but is not limited to, merger, sale, acquisition, financing, transfer and leverage buy-out transactions.
2. It is the policy of the Board that the Executive Director may require a fee in return for granting an assignment when the assignment results in economic or financial benefit to the assignor. Such fee shall be, at minimum, 10% of the economic value attributable to the assignor’s leasehold interest derived from, or a result of, the use of the premises.

#### **VIII. Rates, Fees and Charges**

1. It is the policy of the Board that pricing for use of Port property shall be structured to enhance the Port’s competitive position and advance the Port’s as a positive place to do business while working to achieve minimum Rates Of Return (“ROR”) on land and on improvements consistent with Port financial management policies (currently 10% ROR target on land and 12% ROR target on improvements).
2. It is the policy of the Board that a fixed minimum annual guarantee shall be set for each lease agreement, whereby the Tenant shall pay full or 100% rent while meeting the Port’s return on land and improvements.
3. It is the policy of the Board to establish market rental rates and maximize its ROR through use of appraisals or other pricing methods as may be appropriate. Certain distinguishing factors which may be unique to Port property (for example near- or deep- water proximity, adjacency to heavy rail and transportation routes, and near water accessibility) may be valued using alternative pricing methods.
  - a. Market rental rates shall be established in accordance with the Appraisal Institute’s definition of “market rent” which is *“the most probable rent that a property should bring in a competitive and open market reflecting all conditions and restrictions of the lease agreement, including permitted uses, use restrictions, and tenant improvements.”*

4. It is the policy of the Board that different pricing methods may be used for non-maritime related Lease Agreements.
  - a. Any deviation from market rates and ROR goals intended to encourage tourism, preserve the public's right to fish and to have convenient access to water and other public use must be brought before the Board and approved in open public session.

## **IX. Compensation Adjustments**

1. It is the policy of the Board to require annual adjustments of rental compensation due for all Lease Agreements. Such adjustment shall be designed to cover inflationary and other cost adjustments and be based upon a Consumer Price Index (CPI).
2. It is the policy of the Board that, consistent with the City Charter, compensation resets are required no less often than every five years. Such compensation resets shall be made to the then current applicable fair market rent.
  - a. Any reset to market process shall take into account annual adjustments implemented in preceding periods. However, in no case will any such reset result in adjustments beyond the market rate as such rate is defined in the above Section VIII, Rates, Fees and Charges, 3.a, nor will it result in a reduction to the existing rate.

## **X. Pricing Platform**

1. It is the policy of the Board that pricing for use of Port property shall be structured to enhance the Port's competitive position and that the Real Estate Division shall develop recommendations for pricing of Port property. Such pricing shall be presented to the Board separately for policy adoption. Pricing categories are set forth below.
  - a. Waterfront. Pricing for waterfront property shall consider the area from the pierhead line extending inland to the top of the bank, plus 200 feet inland from the top of the bank. Such pricing shall be set at 100% of the calculated amount and shall be determined per valuation study or appraisal.
  - b. Backlands. Pricing for backlands property shall consider the area beyond 200 feet inland from top of the bank. Such pricing shall be set at 100% of the calculated amount per valuation or appraisal, or 85% of the waterfront value in the event a separate valuation does not exist.

- c. Submerged Lands. Pricing for submerged land shall consider the area from the pierhead line toward the channel line. Such pricing shall be assessed at 33% of the waterfront valuation.
- d. Sub-surface Land. Pricing for sub-surface land area, which has a depth of more than 3 feet beneath the surface, shall be assessed at 50% of the applicable land rate. Pricing for sub-surface land area, which has a depth of less than 3 feet below the surface, shall be assessed at the full applicable rate.
- e. Value of Port-owned properties will be reset every three to five years.
- f. Pricing platforms shall be consistent with all Board adopted financial policies.

## **XI. Security and Environmental Deposits**

1. It is the policy of the Board that Tenants shall provide security for compliance with the terms and conditions of their Lease.
  - a. A standby letter of credit, or equivalent, may be submitted as security for compliance with the terms and conditions of Lease Agreements. The amount shall be determined in relation to the category and term of the Lease Agreement. Two percent of the value of the standby letter of credit or equivalent shall be deducted and paid to a Harbor District maintenance fund and shall be non-refundable.
  - b. The Executive Director may release the standby letter of credit or its equivalent and refund the remaining 98% of the security deposit to the Tenant, provided that Tenant is in compliance with all terms and conditions of the Lease Agreement at the end of the term.
2. It is the policy of the Board that an additional environmental deposit, independent of the security deposit, may be required depending on risk factors associated with the proposed use of the leasehold. Such additional deposit shall be refundable upon compliance with all relevant terms and conditions.

## **XII. Material Deviations**

1. It is the policy of the Board that it shall be advised of all material deviations from the Leasing Policy and that such deviations must be approved by the Board, with findings, in an open public session.
2. It is the policy of the Board that it shall be advised of all material deviations from compliance with a Lease Agreement and that such deviations must be approved by the Board, with findings, in open public session.

3. It is the policy of the Board that the Port may terminate and/or assess Tenants for costs incurred by the Port as a result of unauthorized operation and use under a Lease Agreement, whether such operation or use is material or less than material.

### **XIII. Other Port Plans and Policies**

1. It is the policy of the Board that the Leasing Policy shall comport with other Port policies which cover various financial, environmental and other aspects of property use and entitlement. Applicable Port policies, plans, and standards include, but are not limited to, the Asset Management Policy, Port Master Plan, Historic Structures Policy, Clean Air Action Plan, Hazardous Materials Handling Policy, Storm Water Management Policy, and others as may be appropriate.

### **XIV. Property Ownership**

1. It is the policy of the Board that, unless otherwise negotiated, all Port-owned improvements, fixtures and equipment existing at the commencement of the term of the Lease Agreement shall remain property of the Port. Unless otherwise provided for in the Lease Agreement, title to improvements financed by Tenants or third parties shall revert to the Port upon expiration or termination of the term of the Lease Agreement.
2. It is the policy of the Board to have the discretion to require a Tenant to demolish and remove Tenant-owned improvements and return the leasehold premises to original condition at the Tenant's expense.
3. It is the policy of the Board that in the event the Port ascertains a need to acquire Tenant-owned assets, straight-line depreciation shall be applied to determine the purchase price. Such provision shall be included in the Lease Agreement.

## GLOSSARY OF TERMS

**Appraisal:** A professional opinion or estimate of the value of property. An appraisal is also the act or process of estimating property value.

**Assignment:** Transfer of contractual rights from one contracting party (the assignor) to another party (assignee).

**Capital Investment:** An expenditure that improves the value or extends the life of a major asset.

**Consumer Price Index (CPI):** CPI is an index of change in the price of a representative “market basket” of consumer goods relating to the current price to a designated base year. CPI is used to adjust rent to reflect the impact of economic conditions.

**Executive Director:** The senior Executive Officer of the Harbor Department, appointed by the Mayor of the City of Los Angeles, acting in his/her role and through the authority delegated by the Board of Harbor Commissioners. As used in this Leasing Policy, Executive Director shall mean the Executive Director or Designee as may be from time to time designated to carry out the functions delegated to the Executive Director.

**Harbor Department:** The proprietary department of the City responsible for the management of the Port of Los Angeles and the Harbor District.

**Harbor District:** The lands and waters, and interest therein, under the possession, management and control of the Board<sup>1</sup>.

**Highest and Best Use:** The reasonable and probable use of a property that will support the highest present value of the land.

**Improvements:** Improvements generally include a building or buildings, but may be any permanent structure or other development such as, but not limited to, a street and utilities.

**Land-Use Plan:** Establishes the visions and goals for the development of a specific area and prevents land-use conflicts.

**Market Rent:** As defined by the Appraisal Institute, market rent is “the most probable rent that a property should bring in a competitive and open market reflecting all conditions and restrictions of the lease agreement, including permitted uses, use restrictions, expense obligations, term, concessions, renewal and purchase options, and tenant improvements.”

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<sup>1</sup> Provision of the Los Angeles City Charter Section 651 and the Administrative Code Section 23.49.

**Port Master Plan:** A general plan for long-range development of the Port of Los Angeles, which describes an overall development concept.

**Port Property:** Real property assets, including upland, submerged lands and all improvements thereon, located within the Harbor District which are owned and controlled by the Harbor Department of the City of Los Angeles.

**Premises:** The defined area of control by the tenant which is specified in the lease.

**Pricing Platform:** An established method for calculating the value of an asset.

**Rate of Return:** Rate of return (ROR), also known as return on investment (ROI) is the ratio of money gained or lost (realized or unrealized) on an investment relative to the amount of money invested. The investment may be in the asset or capital.

**Rent:** Consideration paid for the occupancy and use of real property; any consideration not only money.

**Sublease:** A lease from a lessee to another lessee (tenant to another tenant). The new lessee is a sublessee or subtenant.

**Submerged Land:** Submerged land is land that is located underwater.

**Tariff:** Port tariffs prescribe the rates, charges, rules and regulations of the Port of Los Angeles.

**Tenant:** One who has possession of real estate under a lease or other rental agreement.

**Tenant Improvements:** Improvements to land or buildings to meet the needs of the tenant. Such improvements may be new or remodeled, the cost of which may be paid by the landlord, tenant or parts by each.

**Term:** A specified period of time, such as the term of a lease.

**Tidelands:** Tidelands represent the land between the ordinary mean high tide (OMHT) and the mean low tide.

**Waterfront Property:** Waterfront property is located along the edge of the water.