

NETZER & ASSOCIATES

Real Estate Appraisal & Consulting

October 31, 2006

File No. 26-019

Ms. Evelyn Tseng
Revenue Division
City of Newport Beach
3300 Newport Boulevard
Newport Beach, CA 92663

Re: Appraisal Services
Commercial Tidelands – Newport Harbor
Newport Beach, California

Dear Ms. Tseng:

In accordance with your request and based on a review of the information provided on October 16, 2006 entitled “Tidelands Businesses” I have completed further analysis regarding the business uses set forth in the information provided. This letter contains seven pages and is to be considered a supplement to, and read in conjunction with, my October 9, 2006 appraisal, which is identified as File No. 26-019. All of the information included in my prior appraisal, including the Certification, Assumptions and Limiting Conditions, definitions, descriptions and analysis apply to this letter. This letter applies specifically to SECTION B – Commercial Operations (Balboa Island Ferry, Newport Bait Barge) and the additional businesses not previously addressed.

This analysis is completed based on your representation of the “Tidelands Businesses” that are operating in the Harbor and were not specifically addressed in Exhibit A of the Professional Services Agreement. The list of “Tidelands Businesses” is attached to this letter for reference. Based on the list provided, the business’s that are not addressed specifically in my report can be broken down into three main categories: Charters, Boat Rentals and Sport Fishing. It should be noted that based on my review of both the listed businesses and the market data not all of the businesses on the list should be subject to a tidelands lease agreement.

Charters

The following is a summary of the charter businesses that operate in the Harbor, followed by a summary of the relevant market data that applies to the operation of a charter business.

American Yacht Charters
Catalina Passenger Service
Charter Memories
Charter Yachts of Newport Beach
Fun Zone Boat Company
Gondola Romance
Hornblower Cruises and Events

Legend Yacht Charters
Orca Yacht Charters
Pacific Avalon Yacht Charters
Paradiso Yacht Charters
Riverboat Angela Louise
Spirit of Newport
White Light (M.V.)

The “charter” businesses that operate in the harbor provide short-term (less than 24 hour) tours of the harbor and surrounding environs. Some of the charters include catered events including weddings and receptions. In general, they stay within the harbor but some do leave the harbor and provide transportation to and from Catalina Island (Catalina Passenger Service). The following table is a summary of the fees charged by other jurisdictions for charter boat companies that operate in the tidelands.

CHARTER OPERATOR PERCENTAGE RENT RATES SEPTEMBER 2006						
Jurisdiction	San Diego Port	City of Avalon	Santa Barbara	L.A. County	Dana Point	Newport Beach
Charter only	6.0%	7.0%	15%	6.0%	6.0% to 9.0%	6.0%
Food	3.0%					3.0%
Beverage	5.0%					5.0%

Based on the market data uncovered, **I have concluded that market rent for a charter boat operator is 6.0-percent of the gross income from charter boat operations.** If the charter sells or provides food and beverages, including any catered meals as in the case of a wedding reception, **the market rent is 6.0 percent of the charter sales, 3.0 percent of the food sales and 5.0 percent of the beverage sales.** It should be noted that the survey data includes operators that pay these fees to the jurisdiction, with an additional fee for dock space or berthing rights paid to the party that operate the dock/pier and controls the upland/tidelands properties; therefore, and the division of the upland and tideland properties, as is typical in Newport Harbor, is not a factor in this lease arrangement.

Boat Rentals

The following is a summary of the Boat Rental businesses that operate in the Harbor, followed by a summary of the relevant market data that applies to boat rentals.

- | | |
|---------------------|-----------------------------|
| Balboa Boat Rentals | Newport Harbor Boat Rentals |
| Duffy Boats | Newport Jet Sports |
| Marina Sports | Newport Sailing Club |

The market data uncovered is somewhat limited, but the following table summarizes the percentage rents charged in other jurisdictions for the operation of a boat rental business.

BOAT RENTAL PERCENTAGE RENTS SEPTEMBER 2006			
Jurisdiction	San Diego Port	City of Avalon	Los Angeles County
Boat Rentals	10.0%	7.0%	6.0%

Based on the market data uncovered, I have concluded that **the market rent for boat rentals is 7.0-percent of the gross boat rental income.** As with the charter boats the boat rental operations uncovered do not lease directly from the jurisdiction, they rent their dock space from the marina operator; therefore, the division of ownership between the uplands/tidelands does not impact the rental rates.

Sport Fishing

The following is a summary of the Sport Fishing business's that operate in the Harbor followed by the relevant market data that applies to sport fishing operations.

Davey's Locker

Newport Landing

The market data uncovered that pertains to the percentage rents charged for sport fishing operations along the coast is summarized in the following table:

SPORT FISHING PERCENTAGE RENTS					
Jurisdiction	San Diego Port	City of Avalon	City of San Diego	Los Angeles County	Dana Point
Sport Fishing	6.0%	7.0%	7.0%	6.0%	9.0%

Based on the market data uncovered, I have concluded that **the market rent for sport fishing operations is 6.0-percent of the gross income from sport fishing operations.** These operations typically are for either a half-day or for a full day and do not include food and beverages in the ticket price; however, it was reported that many of the sport fishing companies permit the fishermen to bring their own food and drink and that food and drink does not account for a significant source of revenue. They also report that most fishermen have their own tackle and they only sell tackle on the boats as an accommodation and it is not a significant source of revenue either (many have a tackle shop on the upland parcel that accounts for most tackle sales). Based on the market data uncovered the percentage rent (6.0%) applies to all of the revenue associated with the sport fishing operation.

Establishing Base Rent

All of the data presented reflects the total rent being charged but does not address the issue of "Base Rent", or the minimum fixed rent that these businesses pay in conjunction with their leases. In terms of establishing a fixed "Base" or "Minimum" rent for the above business operations, the interviews completed and the lease agreements reviewed indicate that due to the varying physical and locational characteristics (both along the coast and within the individual harbors) of the operations, trying to compare one operators "Base" rent to another is impractical and is not generally an "apples-to-apples" comparison. The most common method of establishing a base rent, or fixed minimum rent, is to take 75-percent of the prior three years gross sales and apply the concluded percentage to this figure. As an example only, the following

methodology is used to establish the base rent for a hypothetical business operating in the tidelands:

Gross Sales 2003:	\$90,000
Gross Sales 2004:	\$100,000
Gross Sales 2005:	\$110,000
Gross Sales – 3 year average:	\$100,000
x 75-percent:	<u>x 0.75</u>
3 year Avg. to apply Percentage:	\$ 75,000
Percentage Rent Factor – 7.0%:	<u>x 0.007</u>
Annual “Base” or “Minimum” Rent:	\$ 5,250

In this example the fixed annual “Base” rent is \$5,250, or \$437.50 per month. The tenant pays the “base” rent either monthly or quarterly, with any “overage” rent paid based on a percent of sales at year end. The overage rent is offset by the fixed annual rent. Using the above figures as an example, and assuming the sales continued the upward trend the total rent in 2006, based on annual sales of \$120,000, would be calculated as follows:

Gross Sales 2006:	\$120,000
x Percentage Rent Factor - 7.0%:	<u>x 0.07</u>
Total Percentage Rent:	\$ 8,400
Less – Fixed Base Rent @ \$5,250:	<u>-5,250</u>
Total Overage Rent Due:	\$ 3,150

In this example, the business operator would pay “overage” rent of \$3,150 based on the percentage clause in the lease.

Other Tideland Operations

As previously noted, the list of “Tidelands Businesses” includes some uses that should not be subject to the market rent conclusions presented in this report and supplement. These are primarily service oriented business operations that are required for the continued use and maintenance of the harbor and, while they may complete most of their business within the tidelands and the harbor, they do not necessarily occupy a fixed location in the harbor. Without these service type businesses that harbor would not be as attractive and the businesses that rely on their services could theoretically loose business and the percentage rent that they pay would be reduced. The following business operations (including the indicated business type) fall into this category and the rent conclusions set forth in this section do not apply. They should be required to have a City Business License and required harbor permits and their fees should be based on city schedules for similar service type operations.

American Marine Oil Systems
Anchor Mooring Company
Barnacle Bills

Boat Maintenance & Environmental
Mooring Service
Bottom Cleaning

Barrett Construction	Pier Construction
Intracoastal Dredging Service	Dredging
Larson's Shipyard	Shipyard
Mobile Harbor Services	Boat Maintenance
Newport Harbor Shipyard	Shipyard
Newport Slip Rentals	Rental of Private Slips
Royal Flush Pumping Service	Boat Maintenance
Shellmaker, Inc.	Mooring Service & Construction
South Mooring Company	Mooring Service
Swift Slip	Pier Construction
Water Works	Bottom Cleaning

Most of these businesses require at least one slip within the harbor to access their clients and would likely pay one of the marina operators for the space.

It should be noted that the above list does not include the yacht sales operations (Bayport Yachts, Johnson Yacht Sales & Olympic Boat Centers) that operate in the harbor. The only market data that I uncovered pertaining to the fees that yacht brokers pay are for the San Diego Port and the City of San Diego. The Port reports that yacht sales in two newly negotiated leases are the greater of \$100 per month or \$5.22 per square foot of land/water per year. The City reports that they charge between 2.0 percent and 4.0 percent of the total commission income from the sales of boats/yachts. In both cases the sale of boats/yachts require the use of both the upland/tideland property and they are generally associated with the operation of a larger marina operation. Given the limited information pertaining to yacht sales it is not possible to draw a conclusion regarding the market rent for a yacht sales operation.

Certification

To the best of my knowledge and belief, I certify that:

The statements of fact contained in this report are true and correct.

The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are my personal, unbiased professional analyses, opinions and conclusions.

I have no present or prospective interest in the property that is the subject of this report, and I have no personal interest or bias with respect to the parties involved.

I have no bias with respect to the property that is the subject of this report or to the parties involved in the assignment.

My engagement in this assignment was not contingent upon developing or reporting predetermined results.

My compensation is not contingent upon the reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value

estimate, the attainment of a stipulated result, or the occurrence of a subsequent event.

The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the Code of Professional Ethics and Standards of Professional Appraisal Practice of the Appraisal Institute, which include the *Uniform Standards of Professional Appraisal Practice*.

The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives.

I have made a personal inspection of the property that is the subject of this report.

No one provided significant professional assistance to the person signing this report.

In accordance with the USPAP Competency Provision, I certify that I have the knowledge and experience to complete this assignment and have appraised this property type before.

Disclosure of the contents of this appraisal review is governed by the Bylaws and Regulations of the Appraisal Institute. In furtherance of the aims of the Institute to develop higher standards of professional performance by its Members, the appraiser may be required to submit authorized committees of said Institute copies of this report and any subsequent changes or modifications thereof.

The Appraisal Institute conducts a voluntary program of continuing education for its designated members. MAI's who meet the minimum standards of this program are awarded periodic educational certification. As of the date of this report, James B. Netzer has completed the requirements under the continuing education program of the Appraisal Institute.

I have personally conducted an inspection of the real property identified in Exhibit A to the Contract For Services, which is the subject of this report. Based upon my investigation and analysis, I have formed the opinion that the subject properties have the following values as of September 30, 2006:

The market rent for a charter boat operator that does not provide food and beverage service is 6.0-percent of the gross income from charter sales.

The market rent for charters that provide food and beverage service is 6.0 percent of the charter sales, 3.0 percent of the food sales and 5.0 percent of the beverage sales.

The market rent for boat rentals is 7.0-percent of the gross boat rental income.

The market rent for sport fishing operations is 6.0-percent of the gross income.

Respectfully submitted,

James B. Netzer, MAI
California General Appraiser No. AG003143

Ms. Evelyn Tseng
October 31, 2006
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Attachment A – Tideland Businesses