



CITY OF EL PASO DE ROBLES
"The Pass of the Oaks"

CITY COUNCIL AGENDA

ADJOURNED REGULAR MEETING

Wednesday March 11, 2009 7:00 PM

**MEETING LOCATION: PASO ROBLES LIBRARY/CITY HALL
CONFERENCE CENTER, 1000 SPRING STREET**

**PLEASE SUBMIT ALL CORRESPONDENCE FOR CITY COUNCIL PRIOR
TO THE MEETING WITH A COPY TO THE CITY CLERK**

**PLEASE REFRAIN FROM CELL PHONE USE DURING THE MEETING
PLEASE TURN RINGER OFF**

7:00 PM – CONVENE REGULAR MEETING

CALL TO ORDER – Downstairs Conference Center

PLEDGE OF ALLEGIANCE

INVOCATION

ROLL CALL Councilmembers John Hamon, Nick Gilman, Ed Steinbeck, Fred Strong, and Mayor Duane Picano

PUBLIC COMMENTS

This is the time the public may address the Council on items other than those scheduled on the agenda. **PLEASE SPEAK DIRECTLY INTO THE MICROPHONE AND BEGIN BY STATING YOUR NAME AND ADDRESS. EACH PERSON AND SUBJECT IS LIMITED TO A 3-MINUTE DISCUSSION.** Any person or subject requiring more than three minutes may be scheduled for a future Council meeting or referred to committee or staff. Those persons wishing to speak on any item scheduled on the agenda will be given an opportunity to do so at the time that item is being considered.

DISCUSSION

1. Proposed Subleases – Kim Lilly Lease

M. Williamson, Assistant City Manager

For the City Council to determine whether the proposed sublease(s) at property leased by Kim Lilly comply with FAA policy.

OPTIONS:

- a. For the City Council to adopt a resolution determining that the evidence in the record regarding ground lease rental rates at other airports for aircraft storage supports a finding that the proposed sublease rents of 17.54 cents per square foot for a five-year sublease term, 16.54 cents per square foot for a one-year sublease term, and 14 cents per square foot for a month-to-month sublease term is fair and reasonable and hereby approves the proposed sublease form submitted by Kim Lilly.
- b. Amend, modify or reject the above option.

ROLL CALL VOTE

ADJOURNMENT:

- THE PCCA TRAINERS DINNER AT THE PASO ROBLES EVENT CENTER IN COMMERCIAL BUILDING NUMBER 2 AT 6:00 P.M., FRIDAY, MARCH 13, 2009
- THE REGULAR MEETING AT 7:30 PM ON TUESDAY, MARCH 17, 2009, AT THE LIBRARY/CITY HALL CONFERENCE CENTER, 1000 SPRING STREET

Any writing or document pertaining to an open session item on this agenda which is distributed to a majority of the City Council after the posting of this agenda will be available for public inspection at the time the subject writing or document is distributed. The writing or document will be available for public review in the City Clerk's Office, 1000 Spring Street, Paso Robles, CA, during normal business hours, and may be posted on the City's web site at <http://www.prcity.com/government/citycouncil/agendas.asp>.

All persons desiring to speak on an agenda item are asked to fill out Speaker Information Cards and place them at the Staff Table prior to public discussion of that item. Each individual speaker will be limited to a presentation total of three (3) minutes per item.

AMERICANS WITH DISABILITIES ACT Any individual, who because of a disability needs special assistance to attend or participate in this meeting, may request assistance by contacting the City Clerk's Office (805) 237-3960. Whenever possible, requests should be made four (4) working days in advance of the meeting.

*THE DEADLINE FOR SUBMITTING ITEMS FOR THE NEXT
REGULAR COUNCIL MEETING IS MARCH 27, 2009*

TO: James L. App, City Manager
FROM: Meg Williamson, Assistant City Manager
SUBJECT: Proposed Subleases – Kim Lilly Lease
DATE: March 11, 2009

NEEDS: For the City Council to determine whether the proposed sublease(s) at property leased by Kim Lilly comply with FAA policy.

- FACTS:**
1. The City and B. Kim Lilly entered into a lease for certain premises at the Paso Robles Airport on March 1, 1979. The lease has been amended and the current term of the lease (the "Lease") expires on July 1, 2033.
 2. The Lease allows Mr. Lilly to use the premises primarily for aircraft storage. There are approximately 46 hangar spaces on the premises, seven of which are owned by Mr. Lilly. For the past several years, he has subleased space to approximately 35 hangar operators, who paid for and installed portable hangars and who also paid for a portion of certain on-site improvements. A number of these subleases expired in August 2007, at which time Mr. Lilly proposed new subleases with rent of 17.5 cents per square foot, which was significantly higher than the rent paid under the existing subleases. The Lease requires that Mr. Lilly submit any proposed subleases to the City for approval. It also requires that Mr. Lilly not impose unreasonable charges or fees.
 3. Staff began receiving telephone calls from several of Mr. Lilly's subtenants complaining that proposed rental increases were well above market rate rents.
 4. Because the Paso Robles airport receives federal funds, the City, as the designated airport sponsor is required to comply with certain Federal Aviation Administration ("FAA") requirements. Among these are FAA Order No. 5190.6A and Grant Assurance No. 22, which require the City to assure that the airport is available to users on fair, reasonable and nondiscriminatory terms.
 5. The City has not previously been required to review proposed rental rates in airport subleases because the parties have generally agreed upon the terms prior to the subleases being submitted to the City for approval. In this case, the City received a number of complaints from similarly –situated subtenants about the proposed rent increases. In addition, no other tenant at the airport has as many subtenants as Mr. Lilly. Because of the subtenants' allegations and the FAA requirements, the City felt compelled to ascertain if the proposed rents were fair, reasonable and nondiscriminatory.
 6. In September 2007, the City requested that Mr. Lilly provide, among other things, documentation that the proposed sublease rents were fair and reasonable, and suggested means by which such documentation could be provided, including comparisons to rents charged at airports comparable to the City's.
 7. The City made it clear to all parties that it did not have the authority to set rents, but only to review them. It also confirmed with the local FAA compliance

officer that its proposed approach of requesting documentation to assure that the proposed rental rates was reasonable and would satisfy the City's obligations under the FAA requirements.

8. In the meantime, Mr. Lilly executed new subleases with a number of subtenants, at the rental rate of 17.5 cents per square foot. However, several of these subtenants claimed they had executed the new subleases under duress since their old subleases were about to expire. However, Mr. Lilly subsequently also entered into agreements extending the terms of the original subleases, at a rental rate of 10 cents per square foot, to allow the parties time to negotiate the terms of a new sublease. Although the term of those extensions expired, the subtenants have remained on site, as month-to-month tenants at the same rental rate.
9. Over several months in 2008, there were several communications between Mr. Lilly and his attorneys, and the attorney for a group of the hangar subtenants, Graham Lyons, and the City. These issues included: (i) the extent of the City's right to review rental rates; (ii) whether Mr. Lilly was in default in the Lease for failing to obtain City approval for certain subleases; (iii) differing interpretations of the FAA requirements; and (iv) what airports were "comparable" to the one in Paso Robles.
10. In August 2008, Mr. Lilly's attorney submitted a letter with a chart showing rents at other airports as evidence to support his proposed rent of 17.5 cents per square foot, for a sublease term of five years. He also proposed rent of 16.5 cents for a one-year term and 14 cents per square foot for a month-to-month sublease. Some of the airports included as comparable facilities were Meadows Field (Bakersfield); El Cajon; Hayward, Van Nuys; Riverside; Mammoth Lakes; Montgomery Field (San Diego) and San Luis Obispo.
11. In October 2008, Mr. Lyons, on behalf of several of Mr. Lilly's subtenants, submitted a letter disputing some of the data gathered by Mr. Lilly's consultant and challenging some of the airports listed as being comparable to Paso Robles. In addition, he stated that it would be very difficult for the subtenants, who have sizable investments in the hangars, to relocate their hangars and therefore they could face significant economic losses. Mr. Lyons proposed that, based on the other rents charged at the Paso Robles Airport, the appropriate rent should be 5.27 cents per square foot, which is less than the rent paid by the subtenants under their original subleases and less than the month-to-month holdover rent.
12. One reason for the disparities in the rental rates quoted by Mr. Lilly's consultant and by Mr. Lyons is that, in addition to the locations of the airports, tenants are paying for different things. In some instances, the tenant is only paying for unimproved square footage, while in other cases, the tenant is actually renting a hangar.
13. The proposed sublease form, as submitted by Mr. Lilly to the City on March 4, makes the textual changes requested by the City. In addition, the proposed rental and terms are as follows:
 - 17.54 cents per square foot – five-year term
 - 16.54 cents per square foot – one-year term

- 14 cents per square foot for month-to-month term

ANALYSIS &

CONCLUSION: As stated above, the City does not have the authority to establish rental rates for airport subleases. As the airport sponsor, however, it does have the obligation to monitor rents and to assure that the fees and charges at the airport, which includes the rents charged to subtenants are fair, reasonable and nondiscriminatory. The information submitted by Mr. Lilly's consultant, even after taking into account the comments from Mr. Lyons' consultant, indicates that the proposed rents for the subleases are within the range of rents charged at other comparable airports.

POLICY

REFERENCE: FAA Order 5190.6A; FAA Grant Assurance No. 22.

FISCAL

IMPACT: No direct fiscal impact to City.

OPTIONS:

- a. For the City Council to adopt a resolution determining that the evidence in the record regarding ground lease rental rates at other airports for aircraft storage supports a finding that the proposed sublease rents of 17.54 cents per square foot for a five-year sublease term, 16.54 cents per square foot for a one-year sublease term, and 14 cents per square foot for a month-to-month sublease term is fair and reasonable and hereby approves the proposed sublease form submitted by Kim Lilly.

- b. Amend, modify or reject the above option.

Attachments:

1. Proposed resolution No. 09 ____
2. Proposed Sublease form, with modifications
3. August 18, 2008 letter from William O'Connor
4. September 11, 2008 letter from William O'Connor
5. October 8, 2008 letter from Graham Lyons
6. October 24, 2008 letter from William O'Connor
7. February 17, 2009 letter from Iris Yang

RESOLUTION NO. 09- _____

RESOLUTION OF THE CITY COUNCIL OF THE CITY OF EL PASO DE ROBLES
FINDING THAT THE SUBLEASE RENTAL RATES AND TERMS PROPOSED BY
B. KIM LILLY ARE FAIR AND REASONABLE AND APPROVING THE PROPOSED
SUBLEASE FORM

WHEREAS, B. Kim Lilly ("Lessee") leases certain premises at the Paso Robles Airport, which lease term extends to July 1, 2033; and

WHEREAS, pursuant to the lease (the "Lease"), Section XII of the Lease provides that the Lessee may not enter into any subleases without the written consent of the City; and

WHEREAS, because the City has received funds from the Federal Aviation Administration ("FAA") and is the designated "airport sponsor" for the Paso Robles Airport, it is required to comply with certain regulations and orders from the FAA (the "FAA Regulations"); and

WHEREAS, FAA Order No. 5190.6A and Grant Assurance No. 22 require the City to assure that the airport is available to users on fair, reasonable and nondiscriminatory terms; and

WHEREAS, for the last several years, Lessee has subleased space on the premises to approximately 35 hangar operators who paid for and installed portable hangars and also paid for a portion of the costs of certain on-site improvements; and

WHEREAS, prior to the expiration of many of those subleases in August 2007, Lessee proposed new sublease terms which included rental rates significantly higher than those then being paid by Lessee's subtenants; and

WHEREAS, several of Lessee's subtenants (the "Subtenants") claimed that the proposed sublease rents far exceeded the fair market rent and were therefore unfair and unreasonable; and

WHEREAS, Lessee and Subtenants executed extensions to their original subleases to provide for time to negotiate mutually acceptable terms, during which extension term Subtenants paid rent of 10 cents per square foot; and

WHEREAS, while the FAA Regulations do not allow the City to establish rental rates for subleases proposed by City's lessees, City believes it has the obligation to monitor such rates to comply with the requirements of the FAA Regulations; and

WHEREAS, because of the complaints from Lessee's subtenants, City requested Lessee to provide evidence that the proposed rental rates and terms for the hangar subleases were fair and reasonable and suggested various methods by which such documentation could be provided, including, but not limited to, ascertaining rents of similar facilities at airports comparable to the Paso Robles Airport; and

WHEREAS, the City confirmed with the FAA compliance division that the City's proposed method of determining whether the proposed sublease terms was fair and reasonable would comply with the City's obligations as the airport sponsor; and

WHEREAS, Lessee provided documentation of rental rates charged to subtenants at other airports which indicated that Lessee's proposed rent of 17.5 cents per square foot was within the range of rents being charged at such facilities; and

WHEREAS, the Subtenants submitted a letter disputing some of the data submitted by Lessee, including data from other airports, and stated their belief that a reasonable rent for the new subleases should be 5.27 cents per square foot, which is lower than that provided in the expired subleases; and

WHEREAS, the disparity in the data submitted by Lessee and Subtenants apparently is due in part to the locations of the airports, whether the subtenants are renting ground space or hangars, and other factors; and

NOW, THEREFORE BE IT RESOLVED by the City Council of the City of El Paso de Robles as follows:

a. The proposed form of Sublease and Modifications to Sublease, attached hereto as Exhibit A and incorporated herein by reference, are approved, provided, however, that Lessee incorporate the Modifications into each executed sublease so that the terms are integrated into a single document; and

b. Based on the evidence submitted, the City Council believes that Lessee's proposed sublease terms do not appear to be unfair, unreasonable or discriminatory. The proposed sublease rents of (i) 17.54 cents per square foot for a five-year sublease, 16.54 cents per square foot for a one-year sublease; and (ii) 14 cents per square foot for a month-to-month sublease are not unfair, unreasonable or discriminatory and are hereby approved.

PASSED AND ADOPTED this 11th day of March 2009, by the following vote:

AYES:

NOES:

ABSENT:

ABSTAIN:

Duane Picanco, Mayor

Attest:

Cathy David, Deputy City Clerk

ATTACHMENT No. 2 to Resolution No. _____

SUBLEASE AGREEMENT

By and Between

**B. KIM LILLY, DBA,
AIRPORT RENTAL AND LEASING COMPANY
Sublessor**

and

Sublessee

DATED: _____

TABLE OF CONTENTS

1.	<u>GRANT AND DESCRIPTION OF PREMISES</u>	1
2.	<u>MASTER LEASE</u>	1
3.	<u>TERM</u>	1
4.	<u>USE OF PREMISES</u>	1
5.	<u>RENTAL</u>	2
6.	<u>SIGNS</u>	3
7.	<u>INSURANCE</u>	3
8.	<u>INSPECTION</u>	4
9.	<u>CONSTRUCTION ON PREMISES</u>	4
10.	<u>PROTECTION OF PREMISES</u>	4
11.	<u>NON-DISCRIMINATION</u>	4
12.	<u>LAWS</u>	5
13.	<u>CONDITION OF THE PREMISES</u>	5
14.	<u>INDEMNIFICATION</u>	5
15.	<u>UTILITIES</u>	6
16.	<u>SUBLETTING AND ASSIGNMENT</u>	6
17.	<u>JOINT USE OF COMMON AREAS</u>	6
18.	<u>INSPECTION</u>	7
19.	<u>CONDEMNATION</u>	7

20.	<u>LICENSES, FEES, AND TAXES</u>	9
21.	<u>TERMINATION CONDITION</u>	9
22.	<u>BREACH</u>	9
23.	<u>NOTICE</u>	9
24.	<u>SUBORDINATION</u>	10
25.	<u>NON-EXCLUSIVE RIGHTS</u>	10
26.	<u>SUCCESSORS</u>	10
27.	<u>MISCELLANEOUS</u>	10
	<u>SIGNATURES</u>	11

SUBLEASE AGREEMENT

By and Between

B. KIM LILLY, dba AIRPORT RENTAL AND LEASING COMPANY
Sublessor

and

Sublessee

Dated: _____

This Sublease Agreement is made and entered into the 1st day of _____, 2007, by and between B. KIM LILLY, dba AIRPORT RENTAL AND LEASING COMPANY (hereinafter referred to as ASublessor@) and _____ (hereinafter referred to as ASublessee@).

1. **GRANT AND DESCRIPTION OF PREMISES:** In consideration of each and every term, covenant, and condition herein contained, Sublessor leases to Sublessee, and Sublessee hires from Sublessor, that certain space situated at the Paso Robles Municipal Airport, located in Paso Robles, California, which space is located on the premises described in that certain lease between the Sublessor and the City of Paso Robles (ACity@) dated March 1, 1979, amended August 1, 1980, May 1, 1987 and October 1, 1988 (the AMaster Lease@). This said Lease was further extended to March 1, 2009 and again to July 1, 2033.

2. **MASTER LEASE:** This Sublease Agreement is made subject to the terms and conditions of the Master Lease. In addition to the terms and conditions of the herein Sublease Agreement, Sublessee agrees to be bound by all of the terms and conditions of the Master Lease.

3. **TERM:** The term of this Sublease Agreement shall commence on _____, and terminate on _____.

4. **USE OF PREMISES:** Sublessor hereby grants to Sublessee the privileges, uses, and rights listed below for performance on the Premises, all of which shall be subject to the terms and conditions and covenants hereinafter set forth; and Sublessee is limited to said privileges, uses, and rights, and shall exercise no other.

A. Under no circumstances may Premises be used for any non-aviation related

businesses or commercial operation, nor for the storage of materials not related to the conduct of aviation related businesses authorized herein, unless otherwise provided for in this Sublease Agreement by attached addendum.

B. **PROHIBITED ACTIVITIES:** The hangar space rented herein shall be used solely for the storage of aircraft and related equipment. The following activities are strictly prohibited:

- a) No parking or storage of motor vehicles or personal equipment shall be permitted in the tie down storage area; however, motor vehicles may be temporarily parked in a hangar when not in use for the storage of an aircraft.
- b) The use of combustible chemicals, welding or similar activities in or adjacent to the storage area is strictly prohibited.
- c) The Sublessee may not conduct any commercial activity in the storage area, unless such use is expressly provided for in an addendum attached hereto.
- d) Any use of the storage area must conform to all Paso Robles Municipal Airport rules and regulations and applicable zoning, building and fire codes.
- e) Any activities which would cause insurance rates on the hangar and adjacent areas to rise.
- f) Any activities which would inhibit the use and enjoyment of adjacent spaces or any part of the airport.
- g) Any modification or alteration of the hangar space without prior written consent of Sublessor.

5. **RENTAL:** Sublessee agrees to pay Sublessor monthly rent plus a utilities fee for the leased space. Payment shall be made monthly in advance, commencing on April 1, 2006.

Rental payment for the Leased Space _____ shall be \$ _____ plus utilities fee per month; the rental payment is due on the 1st day of every month. If the payment is not paid within a five (5) day period, a late penalty of 10% of the rental fee is incurred and due with payment. The rental payment shall be adjusted annually on January 1st according to changes in the Consumer Price Index (CPI) as described below.

Before September 1, 2008, and on and before January 1st of each succeeding year, Sublessor shall notify Sublessee of the change in the CPI for the prior calendar year. If there is a decrease or no change in the CPI during any calendar year then the preceding year=s rent will not be adjusted. Sublessor shall provide at least thirty (30) days prior written notice to Sublessee of each adjusted

rental amount. Failure by Sublessor to notice Sublessee may delay payment of rent but shall not preclude retroactive application of adjusted rent due unless said notice is not provided prior to the expiration of the 12-month period ending the following December 31st.

The term Consumer Price Index (CPI) refers to the Los Angeles-Riverside-Orange County Index for Urban Wage Earners and Clerical Workers based on the period of 1967 equals 100 as published by the Bureau of Labor Statistics of the U.S. Department of Labor. The index for the adjusted date shall be the one reported in the U.S. Department of Labor=s most comprehensive official index then in use and most nearly answering the foregoing description of the index to be used. If it is calculated from a base other than the base period (1967 equals 100), the base figure used for calculating the adjustment percentage shall first be converted under the form as supplied by the Bureau. If the described index is no longer published, another generally recognized as authoritative shall be substituted by agreement of Sublessor and Sublessee. If Sublessor and Sublessee are unable to agree within thirty (30) days after demand by either party on application of either party, the substitute index shall be selected by the Chief Officer of the San Francisco Regional Office of the Bureau of Labor Statistics or its successor.

6. SIGNS: The Sublessee shall not erect or display or permit to be erected or displayed on the rented premises any signs or advertising matter without first obtaining the written approval of the City=s Airport Director. Any signs which the Sublessee desires to install shall be submitted first to the Airport Director for approval as to number, design, size, color and location. The Airport Director shall not approve any sign which is not in harmony with the general plan or the appearance of the Paso Robles Municipal Airport. Consent by the Airport Director shall not relieve the Sublessee from responsibility of hearing to and conforming with any applicable City, State or Federal law, ordinance or regulation thereon.

7. INSURANCE:

A. Liability Insurance: Sublessee shall procure from insurance underwriters satisfactory to the City and the Sublessor a standard form policy or policy of insurance protecting Sublessee, Sublessor and the City against public liability and property damage in a single limit amount of at least One Million Dollars (\$1,000,000.00) per occurrence. Sublessee shall furnish such comprehensive or broad form policies providing combined single limit liability for bodily injury or death and property damage and coverages should be as follows:

1. General and Aviation Liability:

- a. Comprehensive form;
- b. Contractual liability;
- c. Personal injury liability;
- d. Independent contractors working for Sublessee (if required);

e. Hangar keeper=s liability (if not owned aircraft house and hangars). Said hangar keeper=s liability coverage shall be for an amount no less than exposure created by Sublessee=s operation with a minimum coverage of at least Five Hundred Thousand Dollars (\$500,000.00) per loss period.

Any policy shall contain an endorsement naming the Sublessor and the City of Paso Robles and its officers, employees and agents as additional insureds. Sublessee=s insurance will operate as primary insurance and no other insurance affected by the City or Sublessor shall be called upon to contribute to a loss. Upon the request of the Sublessor or the City, Sublessee shall file certified copies of insurance policies with the City. Such insurance certificates shall specifically state and note changes in coverage provided and no cancellation of the policy shall be made without at least thirty (30) days advance notice to Sublessor and the City.

B. Property Insurance: Sublessee shall keep insured with insurance companies acceptable to Sublessor all leasehold improvements to the extent of not less than one-hundred percent (100%) of the full and insurable replacement value against all risk of direct physical loss provided however nothing herein shall require Sublessee to procure earthquake, flood insurance or insurance against any other risk which is not obtainable on a reasonable economic term.

Sublessee shall forward to the Sublessor and the City certificates and policies of required insurance issued by the insurance underwriters evidencing the existence of valid policies, which certificates shall state the coverage will not be amended so as to decrease the protection below the requirements specified nor be subject to cancellation without at least thirty (30) days prior written notice to the Sublessor and the City. Such insurance coverages shall in no way limit the liability of the Sublessee for replacement of improvements.

8. INSPECTION: Sublessor and the City shall have the right with reasonable notice and at reasonable times to inspect the premises for compliance with the terms and conditions of this Sublease Agreement. Included within these inspection rights are the right to inspect inside the hangars, only after Sublessor or the City give Sublessee at least forty-eight (48) hours written notice.

9. CONSTRUCTION ON PREMISES: Any construction, improvement, or alteration must be approved, in writing, by Sublessor prior to commencement of activity.

Title to construction and/or improvements made by Sublessee hereunder shall remain in Sublessee or any legitimate successor or assign subject to Section 21 hereinafter.

Nothing herein shall be construed to be a granting of a waiver of normal permit procedures or requirements as established by the State, County, or other entity of competent jurisdiction, and Sublessee hereby agrees to promptly comply with said procedures or requirements as applicable to

this Sublease Agreement.

10. PROTECTION OF PREMISES: Sublessee agrees to take all reasonable precautions to protect Premises from damage, theft, vandalism, and other such hazards and to adhere to *Federal Aviation Regulations Part 107* for protection of the Premises.

11. NON-DISCRIMINATION: Sublessee will not discriminate against any person or class of persons by reason of race, color, creed, or national origin in the use of any of the facilities provided for the public on the Airport.

12. LAWS: It is understood and agreed that general control over said Airport and all flying activities in connection therewith are vested by law in the City acting by and through its City Council and committees and officers appointed by such City Council. In the general operation of any activities conducted under the terms of this Sublease Agreement, Sublessee agrees to comply with all rules and regulations adopted by the City for the use and operation of the Airport. The laws of the State of California are to be applicable in interpreting this Sublease Agreement.

Sublessee shall, at its sole cost and expense, comply with 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, County, State, and Federal statutes, ordinances, rules, and regulations 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, County, State, and Federal statutes, ordinances, rules, and regulations now in force or which may be hereafter in force. The judgment of any Court of competent jurisdiction, or the admission of Sublessee in any action or proceeding against the City, whether the City be a party thereto or not, that Sublessee has violated any such ordinance, statute, rules, or regulations in the use of the Premises shall be conclusive of the fact as between the City and the Sublessee.

13. CONDITION OF THE PREMISES: Sublessee shall, at all times, keep the Premises in a neat, safe, and sanitary condition, and free of weeds and other noxious growth, and shall, at all times, conduct its operations hereunder in strict compliance with all applicable and pertinent laws, statutes, ordinances, rules, and regulations of all governmental entities and agencies.

Sublessee shall further keep and maintain the Premises and improvements thereon in good order, condition, and repair, reasonable use and wear excepted. Sublessee shall not commit or suffer to be committed on the Premises any nuisance or unlawful act or waste. All painted exterior surfaces and surfaces requiring treatment of any kind shall be maintained in first class condition and

shall be repainted or treated as often as required in order to preserve the structure and maintain high standards of appearance at the site. Any changes in exterior paint color shall be subject to prior written approval of Sublessor who shall be the sole judge of the quality of maintenance.

14. INDEMNIFICATION: Sublessee shall defend, indemnify, and save harmless the Sublessor, the City, its officers, agents, and employees from any and all claims, demands, costs, expenses, or liability occasioned by the performance of the provisions hereof, or in any way arising out of this Sublease Agreement, including but not limited to, inverse condemnation, equitable relief, or any wrongful act, or any negligent act or omission to act on the part of the Sublessee, or of agents, employees, or independent contractors directly responsible to the Sublessee, or of agents, employees, or independent contractors directly responsible to the Sublessee; providing further that the foregoing shall apply to any wrongful acts, or any actively or passively negligent acts or omissions to act, committed jointly or concurrently by the Sublessee, the Sublessee=s agents, employees, or independent contractors and the City, Sublessor, its agents, employees, or independent contractors.

15. UTILITIES: Sublessee shall pay for all utilities used or consumed on the leased premises and installation including, but not limited to, gas, water, electricity, garbage disposal, storm and sanitary sewer service, janitorial service and telephone service. Sublessor will charge **\$10.00** per month for 40 kilowatts of electricity, and Sublessor will monitor usage via an electric meter and charge accordingly for usage above the maximum 40 kilowatts. Rate increases by any of the above-referenced utility companies will be passed on to the Sublessee at the same percent made by said utility companies to Sublessor.

Sublessor reserves the right to adjust the utility charges to the extent necessary to be reimbursed for charges made by utility companies. Sublessor is to be afforded the right to determine the method of apportioning said utility charges in a fair manner between the Sublessees.

16. SUBLETTING AND ASSIGNMENT:

A. Sublessee shall not assign or rent, or relinquish operational control of this Sublease Agreement, or any portion thereof, without the prior written consent of Sublessor in each instance. Said consent by Sublessor shall not be unreasonably withheld. If Sublessor consent to an assignment, a transfer fee of **\$100.00** shall be paid to Sublessor to cover administrative costs in transferring the Sublease and Sublessee shall remain responsible for the performance of all the terms, covenants, and conditions of this Sublease Agreement, including financial obligations to Sublessor. Under no circumstances will the term or conditions of any assignment of this Sublease Agreement exceed the terms or conditions of the Sublease Agreement. If Sublessee assigns said Sublease Agreement, or any portion thereof, without the prior written consent of the Sublessor, then said assignment shall, at the option of Sublessor, immediately cease and terminate.

17. JOINT USE OF COMMON AREAS:

A. The City reserves the right, but shall not be obligated to Sublessee, to maintain and keep in repair the landing area of the Airport and all publicly owned facilities of the Airport, together with the right to direct and control all activities of Sublessee in this regard.

B. There is hereby reserved to the City, its successors and assigns, for the use and benefit of the public, a right-of-flight for the passage of aircraft in the airspace above the surface of the Premises, together with the right to cause in said airspace such noise, smoke, dust, and/or nuisance as may be inherent in the operation of aircraft, now known or hereafter used for navigation or flight in the air, using said airspace for landing at, taking off from, or operating on the Paso Robles Municipal Airport.

C. Sublessee, by accepting this Sublease Agreement, expressly agrees for itself, its successors and assigns, that it will not erect nor permit the erection of any structure or object, nor permit the growth of any tree or vegetation on the Premises, which will exceed the limits established by, nor violate any restriction of the Airport Hazard Zone, as adopted for the Paso Robles Municipal Airport, as it is enacted at the date of this Sublease Agreement, or in the future. In the event the aforesaid covenant is breached, the City reserves the right to enter upon the Premises and to remove the offending structure or object, and to remove the offending tree or vegetation, all of which shall be at the sole cost and expense of Sublessee; and Sublessee hereby agrees to pay to the City the entire cost and expense thereof.

D. Sublessee, by accepting this Sublease Agreement, expressly agrees for itself, its successors and assigns, that it will not make use of the Premises in any manner which might interfere with the landing and taking off of aircraft from the Paso Robles Municipal Airport or otherwise constitute a hazard. In the event the aforesaid covenant is breached, the City reserves the right to enter upon the Premises and cause the abatement of such interference at the sole cost and expense of Sublessee; and Sublessee hereby agrees to pay to the City the entire cost and expense thereof.

18. INSPECTION: The Sublessor and the City shall have the right, with reasonable notice and at reasonable times, to inspect the Premises for compliance with the terms and conditions of this Sublease Agreement.

19. CONDEMNATION:

A. "Condemnation" means (A) the exercise of any governmental power, whether by legal proceedings or otherwise, by a condemnor and (B) a voluntary sale or transfer by Sublessor to any condemnor, either under threat of condemnation or while legal proceedings for condemnation

are pending.

B. "Date of taking" means the date the condemnor has the right to possession of the property being condemned.

C. "Award" means all compensation, sums or anything of value awarded, paid, or received on a total or partial condemnation.

D. "Condemnor" means any public or quasi-public authority, or private corporation or individual, having the power of condemnation.

Section 19.1 - Total Taking - If the Premises are totally taken by condemnation, this Lease shall terminate on the date of taking.

Section 19.2 - Partial Taking - If fifteen percent (15%) of the Premises is taken by condemnation, this Lease shall remain in effect except that Sublessee can elect to terminate this Lease if the remaining portion of the Premises is rendered unsuitable for Sublessee's continued use of the Premises. If Sublessee elects to terminate this Lease, Sublessee must exercise its right to terminate pursuant to this Section 20.2 by giving notice to Sublessor within ten (10) days after the nature and the extent of the taking have been finally determined. If Sublessee elects to terminate this Lease as provided in this Section 20.2, Sublessee also shall notify Sublessor of the date of termination, which date shall not be earlier than thirty (30) days nor later than sixty (60) days after Sublessee has notified Sublessor of its election to terminate; except that this Lease shall terminate on the date of taking if the date of taking falls on a date before the date of termination as designated by Sublessee. If Sublessee does not terminate this Lease within the ten (10) day period, this Lease shall continue in full force and effect, except that minimum monthly rent shall be reduced pursuant to Section 20.3.

Section 19.3 - Effect on Rent - If any portion of the Premises is taken by condemnation and this Lease remains in full force and effect, on the date of taking, the minimum monthly rent shall be reduced by an amount that is in the same ratio to minimum monthly rent as the value of the area of the portion of the Premises taken bears to the value of the entire Premises immediately before the date of taking.

Section 19.4 - Lease Termination - Prevention - If, within ten (10) days after the date that the nature and extent of the taking are finally determined, Sublessor notifies Sublessee that Sublessor, at its costs, will add on to the remaining Premises so that the area and the approximate layout of the Premises, as enlarged, will be substantially the same after the date of taking as they were before the date of taking, and Sublessor commences the restoration immediately and completes the restoration within ninety (90) days after Sublessor notifies Sublessee, this Lease shall continue in full force and effect without reduction in minimum monthly rent, except for any abatement or reduction made pursuant to Section 20.6.

Section 19.5 - Distribution of the Award - The award shall belong to and be paid to Sublessor. The Sublessee's right to receive compensation for damages for its fixtures and personal property and any awards or allowances for relocation and moving expenses, and any awards or allowances for loss or diminution of Sublessee's business, shall not be affected in any manner hereby, and Sublessee shall be entitled to any such awards made for such purposes. Sublessee shall pursue any such award independently of Sublessor and no award to Sublessee shall diminish the award to Sublessor.

For the purposes of this Section, a voluntary sale or conveyance in lieu of condemnation, shall be deemed an appropriation or taking under the power of eminent domain.

Section 19.6 - Temporary Taking - The taking of the Premises or any part of the Premises by military or other public authority shall constitute a taking of the Premises by condemnation only when the use and occupancy by the taking authority has continued for longer than thirty (30) consecutive days. During the thirty (30) day period, all the provisions of this Lease shall remain in full force and effect, except that rent, except for any percentage rent, shall be abated or reduced during such period of taking based on the extent to which the taking interferes with Sublessee's use of the Premises, and Sublessor shall be entitled to whatever award may be paid for the use and occupation of the Premises for the period involved.

Section 19.7 - Waiver - Each party waives the provisions of *Code of Civil Procedure* Section 1265.130 allowing either party to petition the Superior Court to terminate this Lease in the event of the partial taking of the Premises.

20. LICENSES, FEES, AND TAXES:

A. Sublessee shall, and does hereby, assume responsibility for payment of licenses, fees, taxes, etc., applicable to its operation on the Premises.

B. Possessory Interest Tax: The Sublessee hereby agrees to pay his/her prorated share of the possessory interest tax as assessed by the County of San Luis Obispo for the entire lease site area. The prorated share for each lease space shall increase in relation to the increase in the possessory interest tax assessed by the County of San Luis Obispo. Any such imposition of possessory interest tax by any governmental authority shall be a tax liability to Sublessee and any such tax payment shall not reduce any payment due the Sublessor hereunder. Any and all possessory interest tax owed by the Sublessee hereunder shall be owed as additional rent.

21. TERMINATION AND SURRENDER CONDITION: Sublessee accepts the Premises as being in as inspected condition and repair, and agrees to paint, repair, and carpet Premises to proper

standards. Sublessee shall have the right to remove his relocatable metal hangar and other personal property provided that upon such removal Sublessee shall repair at their own expense any damages resulting therefrom. Sublessee agrees, upon the expiration of this Sublease Agreement, or any sooner termination, to peacefully and quietly yield up and surrender possession of the Premises unto Sublessor, its agents or assigns, in as good order and condition as reasonable use and wear will permit.

22. **BREACH**: Notwithstanding any other provisions contained herein, Sublessor and the City may cancel and terminate this Sublease Agreement if Sublessee shall fail, neglect, or refuse to perform and obey any term or condition set forth in this Sublease Agreement, after Sublessor and the City have given to Sublessee written notice of thirty (30) days to do so, unless such failure, neglect, or refusal by its nature cannot be remedied within thirty (30) days of said notice, and Sublessee has within thirty (30) days of the notice commenced, and does thereafter continue, diligent efforts to remedy such failure, neglect, or refusal. Any waiver by Sublessor or the City of any failure by Sublessee to comply with the terms and conditions of this Sublease Agreement shall not be construed to be a waiver by either Sublessor or the City of any similar or other failure by Sublessee to comply with any term or condition hereof.

23. **NOTICE**: All notices to Sublessor shall be given, in writing, personally, or by depositing the same in the United States mail, postage prepaid, and addressed to Sublessor at B.KIM LILLY, dba AIRPORT RENTAL AND LEASING COMPANY, P.O. BOX 1918, PASO ROBLES, CALIFORNIA 93447. All notices to Sublessee shall be given, in writing, by depositing the same in the United States mail, postage prepaid, and addressed to the Sublessee at the current address on file.

Sublessee shall maintain on file with the Sublessor and the City a list and identification of all owners, officers, directors, and persons authorized to sign for Sublessee on official contracts and binding legal documents to include their addresses, telephone numbers, and any further contact information.

Sublessee shall also maintain on file with the Sublessor and the City a list and identification of all aircraft located within the hangar on the leased space, including aircraft identification numbers, type of aircraft and year aircraft was manufactured.

24. **SUBORDINATION**: This Sublease Agreement shall be subordinate to the provisions and requirements of any existing or future agreements between the City and the United States or State of California, or any of them, relative to the operation, maintenance, or development of the Airport. It is further understood that this Sublease Agreement, and all the provisions hereof, shall be subject to whatever right the United States now has, or in the future may have to acquire, affecting the control, operation, regulation, and taking over of said Airport, or the exclusive or non-exclusive use of the Airport by the United States during the time of war or national emergency. During the time of war or national emergency, the City shall have the right to enter into an agreement with the United States for military use of part or all of the Airport. If any such agreement is executed, the provisions of this

Sublease Agreement, insofar as they are inconsistent with the provisions of this agreement with the United States, shall be suspended. Nothing in this Paragraph shall be deemed to be an agreement between Sublessor, the City, and Sublessee that Sublessee, in the event this Sublease Agreement is suspended, waives any rights to compensation Sublessee may have against the United States Government or against the State of California.

25. NON-EXCLUSIVE RIGHTS: Sublessee may not have or enjoy, and may not grant, any exclusive rights of any kind which are forbidden by any applicable and pertinent law, statute, ordinance, rule, or regulation of any governmental entity or agency. It is understood and agreed that nothing herein contained shall be construed to grant, or authorize the granting of, any exclusive right of use which would be in violation of Section 308 of the *Federal Aviation Act* (49 USC, Section 1349).

26. SUCCESSORS: All the terms and conditions hereof shall be binding upon and shall inure to the benefit of the successors, assigns, transferees, and trustees of Sublessor, the City, and the Sublessee.

27. MISCELLANEOUS:

A. This Sublease Agreement sets forth all of the agreements and understandings of the parties and is not subject to modification except in writing.

B. This Sublease Agreement supercedes any and all agreements and leases executed by the parties prior to the effective date of this Sublease Agreement.

C. In the event that any party shall file suit to enforce the terms of this Sublease Agreement, the prevailing party shall be awarded their reasonable attorney=s fees which shall be fixed by the court.

IN WITNESS WHEREOF, Sublessor and Sublessee have set their hands the day and year first above written.

SUBLESSOR:
AIRPORT RENTAL AND LEASING COMPANY

By:

B. KIM LILLY

SUBLEESSEE:

By:

**MODIFICATION OF SUBLEASE AGREEMENT
BY AND BETWEEN**
**B. KIM LILLY, DBA AIRPORT RENTAL AND LEASING COMPANY, SUBLLESSOR
AND**
_____, SUBLLESSEE

This supplemental Agreement made this _____ day of February, 2009 by and between B. Kim Lilly, dba Airport Rental and Leasing Company (hereinafter referred to as "Sublessor") and _____ (hereinafter referred to as "Sublessee").

RECITALS

A. Sublessor and Sublessee made and entered into a written Sublease dated September 1, 2007 to lease Space _____, situated at the Paso Robles Municipal Airport located in Paso Robles, California (the "Sublease"); and

B. The City of Paso Robles (hereinafter referred to as the "Master Lessor"), in order to consent to the Sublease Agreement is requiring certain modifications to the Sublease Agreement; and

C. Sublessor and Sublessee agree to modify the Sublease as provided hereinafter.

THEREFORE, Sublessor and Sublessee agree to modify the Sublease as follows:

1. Section 3: Section 3 on Page 1 shall be amended as follows: "**TERM: The term of this Sublease Agreement shall be as follows:**

- [] A. **A month to month rental agreement commencing _____, 2009 at the rental rate of 14¢ per square foot;**
- [] B. **A one year lease commencing _____, 2009 and ending _____, 2010 at the rental rate of 16.5¢ per square foot;**
- [] C. **A five year lease commencing on _____, 2009 and terminating on _____, 2014 at the rental rate of 17.5¢ per square foot.**

2. Section 5: The first and second paragraph of Section 5 shall be amended as follows: "**RENTAL: Sublessee agrees to pay Sublessor a monthly rent plus the utility fees for the leased space. Payment should be made monthly in advance commencing on _____, 2009.**

Rental payment for the leased/rented Space _____ shall be \$ _____ plus utility fee per month; the rental payment is due on the first day of every month. If the payment is not paid within five (5) days, a late penalty of 10% of the rental fee is incurred

and due with payment. The rental payment shall be adjusted annually on January 1st according to changes in the Consumer Price Index (CPI) as described below.

The first sentence of the second paragraph of Section 5 on Page 2 shall be amended as follows: **"Before September 1, 2008 and on or before the first of each succeeding year, Sublessor shall notify Sublessee of the change in the CPI from the prior calendar year."** The rest of the paragraph shall remain the same.

The first sentence of the third paragraph of Section 5 on Page 2 shall be amended as follows: **"The term Consumer Price Index (CPI) refers to the San Francisco-Oakland-San Jose index for urban wage earners and clerical workers based on the period of 1967 equals 100 as published by the Bureau of Labor Statistics of the U.S. Department of Labor."** The remainder of the paragraph shall remain the same.

3. Paragraph 6 on Page 3 shall be amended to read as follows: **"SIGNS: The Sublessee shall not erect or display or permit to be erected or displayed on the rented premises any signs or advertising matter without first obtaining the written approval of the City Planning Department. Any signs which Sublessee desires to install shall be submitted first to the City Planning Department for approval as to number, design, size, color and location. The City Planning Department shall not approve any sign which is not in harmony with the general plan or the appearance of the Paso Robles Municipal Airport. Consent by the City Planning Department shall not relieve the Sublessee from responsibility of heeding to and conforming with any applicable City, State or Federal law, ordinance or regulation thereon."**

4. Section 9: The second paragraph of Section 9 on Page 4 shall be amended to read as follows: **"Title to construction and/or improvements made by Sublessee hereunder shall remain in Sublessee or any legitimate successor or assign of Sublessee subject to Section 21 hereinafter."** The rest of Section 9 shall remain the same.

5. Section 12: The following paragraph shall be added to Section 12: **"Sublessee, for himself, his heirs, personal representatives and assigns as a part of the consideration hereof, does hereby covenant and agree, as a "covenant running with the land", that in the event facilities are constructed, maintained or otherwise operated on said property described in this lease for a purpose for which a DOT program or activity is extended or for another purpose involving the provision of similar services or benefits, Sublessee shall maintain and operate the Premises in compliance with all other requirements imposed pursuant to title 49, part 21, Non-Discrimination and Federally-assisted programs of the Department of Transportation Effectuation of Title VI of the Civil Rights Act of 1964, as said regulations may be amended."**

6. Sections 19.1, 19.2, 19.3 and 19.4: All references to the term "Lease" are hereby revised to refer to **"Sublease."**

7. Section 21: Section 21 shall be amended as follows: "**TERMINATION AND SURRENDER CONDITION:** Sublessee accepts the Premises as being in as inspected condition and repair, and agrees to paint and repair Premises to proper standards. Sublessee shall have the right to remove his relocatable metal hangar and other personal property provided upon such removal, Sublessee shall repair at their own expense any damages resulting there from. Sublessee agrees upon the expiration of this Sublease Agreement or any sooner termination to peacefully and quietly yield up and surrender possession of their Premises unto Sublessor, its agents or assigns, in as good order and condition as reasonable use and wear will permit."

9. In all other respects, said Sublease, together with this Modification of Sublease shall continue in full force and affect. This Modification of Sublease shall become effective as of _____, 2009.

SUBLESSOR:

B. KIM LILLY, dba AIRPORT RENTAL -
AND LEASING COMPANY

By: _____

SUBLESEE:

By: _____

ATTACHMENT NO. 3 to Resolution No. _____

MORRISON | FOERSTER

12531 HIGH BLUFF DRIVE
SUITE 100
SAN DIEGO, CALIFORNIA
92130-2040
TELEPHONE: 858.720.5100
FAXIMILE: 858.720.5125
WWW.MFO.COM

MORRISON & FOERSTER LLP
NEW YORK, NEW YORK 10019
LOS ANGELES, CALIFORNIA
SAN DIEGO, WASHINGTON, D.C.
NORTHERN IRELAND,
GRANGE COUNTY, IRELAND
SACRAMENTO, BALTIMORE, GREEN
BAY, MILWAUKEE, MADISON,
DETROIT, ANN ARBOR, BIRMINGHAM,
PHILADELPHIA, NEW YORK,
SINGAPORE, BRUSSELS

August 18, 2008

Writer's Direct Contact
858.720.7932
WOConnor@mfo.com

Iris P. Yang, Esq.
McDonough Holland & Allen PC
555 Capitol Mall, 9th Floor
Sacramento, CA 95814-4692

Re: Kim Lilly - Subleases at Paso Robles Airport

Dear Ms. Yang:

Enclosed please find the letter from our consultant, John Milligan. In Mr. Milligan's expert opinion, the proposed rental rate of 17.5 cents is consistent with the FAA's Final Policy Regarding Airport Rates and Charges ("FAA Policy"). 61 Fed.Reg. 31,994 (June 21, 1996) and FAA.¹

Presently there are 13 tenants who have executed subleases with Mr. Lilly.² Of these 13 tenants, eight did not enter into lease extensions nor have they claimed that the fully executed subleases are invalid or contain objectionable rates. Thus, we are requesting that the City consent to these eight subleases as soon as possible.³ If the City will not approve these subleases, we are requesting a written explanation as to why consent is being withheld.

With respect to hangar tenants who have not executed subleases, Mr. Lilly will be offering the following terms to any subtenant who wishes to execute a new sublease.

¹ For additional information regarding the relevant FAA Policy please see my letter to Ms. Williamson of April 1, 2008 attached at Tab A.

² The following subleases were submitted for approval on April 1, 2008: Pete Johnson Chevrolet, Hastings Ranch Vineyard, Eberle Winery, Chris Henry, William Hurst, Kenneth Finch, Rodney Dykhouse, John Dolan, James Rossi, Koke Construction, Jim Judd, Hogue Bros. Inc., and Black Oak, Inc. In an email to me, Mr. Lyons claims to represent John Dolan, Rodney Dykhouse, James Rossi, Koke Construction, and Kenneth Finch. Only Mr. Lyons' clients have objected (after the fact) to the proposed rate and now claim the sublease was obtained under duress or voided by the extensions.

³ Mr. Glick will be submitting four additional subleases to the City under separate cover relating to Aero Services and John Moore.

MORRISON | FOERSTER

Iris P. Yang, Esq.
August 18, 2008
Page Two

17.5 cents per square foot for 5-year lease term;
16.5 cents per square foot for 1-year lease term; and
14 cents per square foot for month-to-month lease term.

We will begin discussing directly with the subtenants new subleases based on the terms listed above. Because we are confident, based on Mr. Milligan's opinion, that the proposed rates are reasonable and comply with FAA Policy, we see no reason to delay direct negotiations with the subtenants.

As for the remaining hangar tenants currently represented by Mr. Lyons, we intend to negotiate with them as soon as we have obtained agreement from the other tenants.

Very truly yours,

William V. O'Connor

William V. O'Connor

Enclosure

Tab A

JOHN P. MILLIGAN
24652 Priscilla Drive
Dana Point, CA 92629

August 18, 2008

William V. O'Connor
Morrison & Foerster LLP
12531 High Bluff Drive, Suite 100
San Diego, CA 92130

Re: Paso Robles Airport/Kim Lilly

Dear Bill:

You have asked me to review certain documents regarding leasing/subleasing rates and procedures at Paso Robles Airport having to do with the master leasehold of Mr. Kim Lilly. I offer the following information.

As you are aware, I have over 25 years experience with the Federal Aviation Administration (FAA) serving in the Western-Pacific Region, Airports Division and the office now known as the Los Angeles Airports District Office. I am a registered civil engineer in the state of California. As FAA Airports Engineer and the supervisor of that office, I administered the Airport Improvement Program, which entailed providing grant funding for airport development, applying construction and safety standards, and ensuring compliance with airport sponsors' obligations and assurances. The Los Angeles office is responsible for airports in Southern California and Arizona. I have extensive experience in assisting airport sponsors, consultants and airport tenants in meeting those obligations.

I have reviewed the correspondence between the City of Paso Robles, representatives of several subtenants, representatives of Mr. Lilly and other information regarding Paso Robles Airport and the subject proposed lease rates within the Airport Rental and Leasing leasehold on the airport.

Airport Information

According to the website for the airport maintained by the City of Paso Robles, the airport harbors almost 200 based aircraft. The California Department of Forestry Air Attack Base provides fire protection for Central California. The California Highway Patrol Air Operations Division provides search, patrol, and enforcement services within 100 miles of the airport. Military, air charter, air ambulance, and other aeronautical services operate from the airport on a regular basis. The airport's 1,300 acres includes its industrial park with almost 500,000 sq. ft. of industrial building in operation in nearly 40 industrial businesses.

William V. O'Connor
August 18, 2008
Page Two

Two runways are available for use. Runway 1-19 is 6,000 feet by 150 with pavement strength weight bearing capacity is 60,000 pounds for aircraft with single wheel landing gear configuration, 106 K lbs for dual, and 150 K lbs for dual-tandem. This runway has high intensity runway edge lights. Runway 13-31 is 4,700 feet by 100 feet with pavement strength 30 K lbs for single, 50 K lbs dual wheel and 90 K lbs dual-tandem.

Three non-precision instrument approach procedures are available for use on Runway 19 using the Paso Robles VORTAC and GPS.

The airport has approximately 135 aircraft hangars, 95 aircraft tie-down positions, a jet aircraft charter service, a fuel vender, and four maintenance services.

Issues

Mr. Kim Lilly is a master leaseholder at Paso Robles Airport. The City leases a hangar development site with access to the public taxiway and runway system to Mr. Lilly. Mr. Lilly in turn subleases individual hangar sites to owners of portable hangars. Subleases that Mr. Lilly offers for the benefit of the subtenants have recently expired. Mr. Lilly has offered renewal terms at rates considered by Mr. Lilly to be fair and reasonable. Subtenants, wishing terms more favorable to themselves, have complained to the City that the proposed terms may not be in compliance with FAA requirements. The City has requested that Mr. Lilly provide documentation that the proposed rates are reasonable and in compliance with FAA requirements in the form of comparable rates at similar businesses at similar airports. The City desires this information from Mr. Lilly to "prove" that the proposed rates are in compliance with FAA requirements.

Background

The City of Paso Robles, as owner/operator of the Paso Robles Airport, has accepted federal obligations incorporated in the FAA grant agreements and conditions in the airport's deed of transfer from the federal government. These obligations include the requirement that rates, fees, and charges at the airport must be (1) fair and reasonable, (2) not unjustly discriminatory, and (3) to the extent possible, the result of local negotiation and agreement. The obligation for reasonable rates and charges rests with the airport sponsor and does not extend to airport tenants. This is why it is prudent for a sponsor, as the City has with Mr. Kim's lease, to require its master tenants to gain sponsor approval for lease and rental rates so that the sponsor holds control of rates on its airport. However, I am not aware of an instance where a sponsor has expected a master tenant to "prove" that proposed rates are comparable to like kind arrangements at other airports as the City has demanded of Mr. Lilly. Common practice is to allow the master tenant and proposed subtenants to negotiate rates by agreement without interference by the airport sponsor.

William V. O'Connor
August 18, 2008
Page Three

The intent of the FAA Airport Rates and Charges Policy (and exclusive rights prohibition) is to promote and protect fair competition at public use airports. Since airports are not alike and leaseholds on an airport are typically different in size and activity (business or otherwise), FAA will not ordinarily question the fairness of rates and charges to Fixed Base Operators or other airport tenants unless complaints have been made alleging that specific practices are unfair or unreasonable, and supported by factual evidence produced by the complainant. Rarely can it be established that a rate is so high that it would recover an unreasonable amount. More often, the FAA will act to determine whether the rate structure will result in discrimination.

The FAA finds that the provision of aircraft storage and aircraft service is best accomplished by profit motivated private enterprise. It recognizes that leaseholds and activities in those leaseholds are generally not comparable from airport to airport, or within the same airport. One operator may lease infrastructure improvements and another builds its own facilities, providing justification for different rental and fee structures. If one operator is in a prime location and another is in a less advantageous area, there could logically be a differential in charges. It is expected that an individual operator, such as Mr. Lilly, should offer similar rates for similar ground rents so that there is no appearance of unfair discrimination toward his own subtenants. For these reasons, attempting to compare the proposed rates with existing rates for comparable facilities in similar business and economic conditions is difficult. This is why FAA policy prefers that market rates are best arrived at by agreement, through direct negotiations with proposed subtenants (for a complete discussion of FAA policy, see W. O'Connor's letter to the City dated April 1, 2008.) However, I have contacted Mr. Bill Ingraham, who has related three strikingly similar situations at comparable airports in California that are useful for our analysis. Mr. Ingraham presently manages San Bernardino Airport, and has previously managed the San Bernardino County Airports Department, and Oklahoma City Airport.

First, Lance Air (Lance or Ellen Ricotta) is a master tenant leasing ground at Chino Airport with a situation similar to Airport Rental and Leasing Company. Chino Airport serves a general aviation mix of aircraft owners and businesses and is one of the few locations that allow Port-A-Ports in Southern California. Lance Air leases 3.2 acres of paved ramp at the current rate of \$2673 per month. This equates to \$0.019 per square foot for the master tenant. Lance Air owns a few of the hangars which, in turn, are rented for aircraft storage with subtenants renting both hangar and ground. Lance Air leases ground to several other individual portable hangar owners at rates that vary but are generally around \$150 per month, which equates to approximately \$0.18 cents per square foot.

Secondly, Atlantic Aviation is a master tenant leasing ground at Bakersfield Meadows Field with a situation similar to one described at Paso Robles. Atlantic Aviation is establishing a new rate \$0.25 per square foot, up from \$0.15. The rate is charged on the actual space

William V. O'Connor
August 18, 2008
Page Four

occupied by a hangar structure and excludes any ramp areas much like the situation at Paso Robles.

Third, at Riverside Municipal Airport, similar facilities are offered at a rate of \$0.175 to \$0.22 cents per foot. I have reviewed Fred Glick's letter of January 10, 2008 to the City, and discussed with Mr. Lilly the situation at Riverside Airport. Fred Glick offers to Meg Williamson information on a ground lease situation held by Mr. Lilly and himself that is most similar to that at Paso Robles in his letter dated January 10, 2008. Since Mr. Lilly is a principal, the Riverside example may be most directly comparable to the Airport Rental & Leasing consideration.

In addition, I have attached a table that summarizes from a number of airports surveyed in California that, similar to Mr. Lilly's business at Paso Robles Airport, where aircraft operators own their hangars and lease the ground from a master leaseholder. These thirteen examples receive rates, while varying widely, that are in the range of rates Mr. Lilly is proposing at Paso Robles.

The prime obligation of an airport sponsor is to operate the airport for the use and benefit of the public. While the City of Paso Robles is not required to construct aircraft storage hangars, it has the obligation to make available suitable areas or space on reasonable terms to those who are willing and qualified to construct or otherwise establish such aircraft support facilities. This is the action the City has taken in the case of Mr. Lilly's ground leasehold. In keeping with the expectation that profit motivated fair competition best provides reasonable rates, the City could now undertake its option to provide other space on the airport for a subtenant, who is unable to arrange satisfactory terms with Mr. Lilly, to relocate elsewhere on the airport at his own expense, assuming such space is available.

One of the issues raised by the City relates to compliance with FAA Order 5190.6A, Airport Compliance Requirements. In my review, I find a misunderstanding on the City's part of the applicability of FAA orders to the present situation. This document is not regulatory and is not controlling with regard to airport tenant conduct (or even sponsor conduct). It establishes the policies and procedures to be followed by FAA personnel in carrying out the FAA's responsibilities for ensuring sponsor compliance with its obligations. Clearly, this order does provide very good information for sponsors in understanding basis and details of their obligations. However, incorporating the order into lease terms would not be considered appropriate.

Conclusion

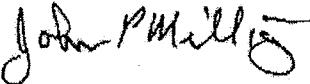
In my opinion, the representatives of the subtenants have not provided evidence that the proposed rates offered by Mr. Lilly are unfair or unreasonable. The subtenants are not bound to accept the terms offered. They hold their option to relocate their hangars elsewhere on the

William V. O'Connor
August 18, 2008
Page Five

airport (or at another airport) on terms they may negotiate with the City or other businesses. Should the City accept and approve the proposed rate of \$0.175 cents per square foot and the FAA be caused to review the proposed lease rate, I do not believe the FAA would take exception under its Airport Compliance Program. Likewise, the City should not take exception proposed rates based on the parallel language contained in Section III of Mr. Lilly's lease.

If I can be of further assistance, please don't hesitate to ask.

Sincerely,



John P. Milligan

Attachment

Survey of airport ground lease/hangar ownership

	Ground lease rate/month Proposed	New	Existing	Location	Contact	Phone #
0.25	0.125 Apple Valley Airport				Joe	(760)247-57--
	0.15 Meadows Fd/Bakersfield				Mr. Cecil	(616)391-4906
	0.17 Chino Airport			Lance Air	Tom Ricotta	(619)987-6656
	0.108 Buchanan Fd/Concord				Julie	(925)646-5722
0.21	0.19 El Cajon Airport (Gillespie Fd)				Cindy	(619)562-3040
0.214	Hayward Air Terminal				Gary Briggs	(925)200-0247
	0.1625 Fox Fd/Lancaster				Steve Erving	(661)940-1709
0.54	0.3 Van Nuys Airport				Bob Fickel	(818)705-9861
0.26	Hawthorne Airport					
0.1675	Mammoth Lks Airport				Pat	(760)924-9127
	0.2 Riverside Muni Airport				Sharon	(805)544-2450
0.29	0.144 Montgomery Fd/San Diego				Kevin	(858)277-1453
	0.21 Palomar-McClellan Airport/Carlsbad					
0.21	0.19 Brown Fd/San Diego					
	0.07 San L Obispo Co Airport					
	0.12 Thermal Airport				Peggy Nelson	(760)399-4300

\$0.17 Average ground lease rate, based on sum of surveyed rates at airports, divided by number of airports (2.1395/13)

\$0.27 Average proposed new lease rate, based on sum of surveyed rates at airports, divided by number of airports (2.1,

The above summarises a survey by Kim Lilly of aircraft hangar storage facilities at airports with a master leaseholder subleasing land to individual tenants who own their hangars with no reversion of structure at end of lease term.

Survey of airport ground lease/hangar ownership

415/8)

The above summarises a survey by Kim Lilly of aircraft hangar storage facilities at airports with a master leaseholder subleasing land to individual tenants who own their hangars with no reversion of structure at end of lease term.

MORRISON

| FOERSTER

12531 HIGH BLUFF DRIVE
SUITE 100
SAN DIEGO, CALIFORNIA
92130-2040
TELEPHONE: 858.720.5100
FACSIMILE: 858.720.5125
WWW.MOFO.COM

MORRISON & FOERSTER LLP
NEW YORK, SAN FRANCISCO,
LOS ANGELES, BALTIMORE,
SAN DIEGO, WASHINGTON, D.C.
NORTHERN VIRGINIA,
ORANGE COUNTY, DENVER,
SACRAMENTO, SANTA CRUZ
TOKYO, LONDON, BEIJING,
SINGAPORE, BRUSSELS

July 25, 2008

Writer's Direct Contact
858.720.7932
WOConnor@mofo.com

Iris P. Yang, Esq.
McDonough Holland & Allen PC
555 Capitol Mall, 9th Floor
Sacramento, CA 95814-4692

Re: Kim Lilly - Subleases at Paso Robles Airport

Dear Ms. Yang:

This will acknowledge receipt of your July 3, 2008 letter and respond to certain matters contained therein. Please note that the letter was not received in my office until July 8, 2008 due to the holiday weekend. In the future, please send all correspondence by fax or email.

We appreciate the City's clarification regarding the February 14, 2008 letter from Ms. Williamson. On the basis that the City does not consider Mr. Lilly to be in default of the Master Lease, we are going forward with our preparations for a comprehensive proposal justifying a rental rate increase at the Airport. We will be in a position to forward the proposal to City very soon, but I would appreciate some flexibility regarding the timing of the submission on account of the five days that were lost in the transmission of the letter and the significant time and effort required to complete the proposal in accordance with the City's demands. I am meeting with our consultant, John Milligan, early next week to discuss the preliminary results of his comprehensive airport survey and I will be in a position to update you on our progress at that time.¹

Your letter implies that the delay in resolving the issue with Mr. Lilly's tenants is due to the death of Mr. Lilly's wife. Frankly, Mr. Lilly was personally insulted by that remark and it has no basis in fact. The delay can be attributed to the City injecting itself into the dispute and the tenants' refusal to negotiate in good faith. For example, Mr. Lyons first proposed a rental rate that was less than what the hangar tenants paid in the mid-eighties and then he refused Mr. Glick's offer of mediation when the City sent the February 14, 2008 claiming Mr. Lilly was in default of the Master Lease. Moreover, there have been multiple month-long delays by the City in responding to our requests to approve subleases. I can appreciate

¹ As you know the hangar situation on Mr. Lilly's leasehold is quite unique. We are looking into airports around the country where the tenants own the physical hangar and lease the ground from someone else.

MORRISON | FOERSTER

Iris P. Yang, Esq.

July 25, 2008

Page Two

that the City prefers not to have holdover tenants at the Airport, but to suggest that Mr. Lilly is to blame for the current situation is completely false.

Finally, Mr. Lilly does not agree with your characterization of the legal effect of the sublease extensions. We believe that the new subleases Mr. Lilly proposed were valid and complied with FAA policy and guidelines regarding rates. Therefore, we reserve all rights with respect to that issue in the event these issues cannot be resolved amicably following our proposal to the City and the tenants.

I look forward to updating you next week on the status of the proposal.

Very truly yours,



William V. O'Connor



McDonough Holland & Allen PC
Attorneys at Law

Iris P. Yang
Attorney at Law

Sacramento Office
916.325.4576 tel
916.444.3826 fax
iyang@mhalaw.com

July 3, 2008

William V. O'Connor
Morrison & Foerster LLP
12531 High Bluff Drive, Suite 100
San Diego, CA 92130-2040

Re: Paso Robles Airport – Kim Lilly Lease

RECEIVED

JUL 07 2008

MORRISON & FOERSTER LLP
SAN DIEGO

Dear Bill:

As we discussed recently, your client, Kim Lilly, has indicated that he is willing to prepare a counterproposal to that proposed by some of Mr. Lilly's hangar subtenants if he can be assured by the City of Paso Robles that the City does not consider him to be in default of his lease (the "Master Lease") with the City.

The purpose of this letter is to advise you that the February 7, 2008 letter sent by Meg Williamson, Assistant City Manager, to Mr. Lilly, is not considered by the City to be a formal notice of default pursuant to which the City intended to exercise its right to terminate the Master Lease. The letter was meant to remind him that the Master Lease provides that any assignment or sublease of any portion of the property must be approved by the City. It was written in response to a November 1, 2007 letter that Ms. Williamson had received from Fred Glick, another attorney representing Mr. Lilly, regarding new five-year subleases that apparently had been executed by the parties but had not been approved by the City. However, as you know, Mr. Lilly also then subsequently executed four-month extensions of the original subleases with the same subtenants, actions that voided the new subleases. The stated purpose of the sublease extensions was to provide time for the parties to agree upon new sublease rents. It is our understanding that those sublease extensions expired on December 31, 2007, and that the subtenants remain on their respective sites as holdover tenants.

As mentioned in Ms. Williamson's letter, the City, as an Airport Sponsor, has both the authority and the obligation to review sublease terms, including proposed rental rates, to ensure that they are reasonable. She requested that Mr. Lilly provide evidence that is reasonably satisfactory to the City that the proposed rental rates for the hangars are comparable to those being charged at other airports with similar facilities and services and/or within similar market areas. In our last conversation, you stated that Mr. Lilly

Sacramento
555 Capitol Mall
9th Floor
Sacramento CA
95814-4692
tel 916.444.3900
toll free 800.403.3900
fax 916.444.8334

Oakland
1901 Harrison Street
9th Floor
Oakland CA
94612-3501
tel 510.273.8780
toll free 800.339.3030
fax 510.839.9104

www.mhalaw.com

1110130v1 32866/3004



McDonough Holland & Allen PC
Attorneys at Law

July 3, 2008
Page 2

would utilize these criteria, but may also use other factors as well in developing a counterproposal.

We understand and appreciate that there were personal family matters that required Mr. Lilly's attention in the last few months. However, we believe that there must be a resolution of these sublease issues very soon, as the City cannot indefinitely sanction having numerous holdover tenants at the airport. By requiring City approval of subleases, the Master Lease does not contemplate a situation where there are long-term holdover tenants. To that end, we must insist that Mr. Lilly present, within thirty (30) days of the date of this letter, a counterproposal to the subtenants whose subleases have expired along with the supporting documentation that the proposed rental rates are reasonable. A copy should also be sent to Meg Williamson.

We appreciate your cooperation in this matter. Please let me know if you have any questions.

Very truly yours,

A handwritten signature in cursive script, appearing to read "Iris".

Iris P. Yang

IPY:jjh

cc: James L. App, City Manager
Meg Williamson, Assistant City Manager
Roger Oxborrow, Airport Services Coordinator
Graham M. Lyons, Esq.

12531 HIGH BLUFF DRIVE
 SUITE 100
 SAN DIEGO, CALIFORNIA
 92130-2040
 TELEPHONE: 858.720.5100
 FACSIMILE: 858.720.5125
 WWW.MOFO.COM

MORRISON & FOERSTER LLP
 NEW YORK, SAN FRANCISCO,
 LOS ANGELES, PALO ALTO,
 SAN DIEGO, WASHINGTON, D.C.
 NORTHERN VIRGINIA,
 ORANGE COUNTY, IRVINE,
 SACRAMENTO, WALNUT CREEK
 TOKYO, LONDON, BEIJING,
 SHANGHAI, HONG KONG,
 SINGAPORE, BRUSSELS

April 29, 2008

Writer's Direct Contact
 858.720.7932
 WOConnor@mofo.com

Iris P. Yang, Esq.
 McDonough Holland & Allen PC
 555 Capitol Mall, 9th Floor
 Sacramento, CA 95814-4692

Re: Kim Lilly - Subleases at Paso Robles Airport

Dear Ms. Yang:

Thank you for your April 7, 2008 letter and I look forward to discussing a possible framework to resolve the issues regarding the approval of Mr. Lilly's subleases with hangar tenants at the Paso Robles Airport. Your letter, however, raises additional issues that need to be addressed before any meaningful discussions can occur.

First, I understand that there are seven tenants that entered into new subleases ("New Subleases") with Mr. Lilly prior to hiring Mr. Lyons. After those seven tenants (along with numerous other tenants) retained Mr. Lyons, Mr. Lyons negotiated with Mr. Glick, Mr. Lilly's attorney, an extension to the original sublease agreement ("Original Sublease") so that the parties could attempt to resolve a mutual rental rate for the New Subleases. Since Mr. Lyons and the City take the position that the New Subleases are not effective until the City approves them, the extension of the Original Subleases seems to be the proper way to handle the time gap between the expiration of the Original Subleases and the City consenting to the New Subleases. Unfortunately, Mr. Lyons then proposed a rental rate of 5.63 cents per square foot which is less than the rental rates the tenants paid in 1985. Obviously Mr. Lyons and his clients never intended to negotiate in good faith, breaching a material term of the lease extensions, and the lease extensions were therefore allowed to expire December 31, 2007.

What is particularly troublesome is the fact that in your correspondence you have taken the position that the New Subleases entered into between Mr. Lilly and Mr. Lyons' seven tenants are void. I would respectfully suggest that this is not your position to take. If there is a disagreement between Mr. Lyons and my client, Mr. Lilly, concerning the enforceability of the New Subleases, that will be adjudicated by a San Luis Obispo County Superior Court Judge. We will clarify with Mr. Lyons and ask him to confirm in writing that it is the position of his clients that the extensions nullified the New Subleases. Until we know where we stand with Mr. Lyons' clients, I do not believe negotiations with the City will be

Iris P. Yang, Esq.

April 29, 2008

Page Two

productive. In the meantime, we have submitted all of the subleases that Mr. Lilly has entered into with various subtenants for the City's consent. There does not seem to be any objection at this point to the Sublease form itself, and the only matter that the City has indicated that is still up in the air with regard to the Subleases is the rental rate.

Second, the City acknowledges that the City has no authority or desire to set lease rates for subleases at the Paso Robles Airport. In the next breath, however, your letter implies that we are required to prove the rental rates are reasonable according to data that the City has unilaterally determined is required, i.e., similar airports and similar facilities. As stated in my previous letter of April 1, 2008, there is nothing in the FAA Policy that requires Mr. Lilly to carry the burden on this point or to provide this data to establish that the proposed rate of 17.9 cents per square foot is reasonable. With the foregoing in mind, we are requesting that the City consent to the Subleases that have been previously provided. If in fact the City refuses to consent to those Subleases, we request they do so in writing and state the reasons for withholding consent.

Finally, your letter fails to acknowledge that Mr. Lilly is not in default of the Lease. Mr. Lilly was informed by Ms. Williamson that there is no Notice of Default pending. However, I am requesting that you confirm this as well.

Very truly yours,



William V. O'Connor

MORRISON | FOERSTER

Iris P. Yang, Esq.

April 29, 2008

Page Three

bcc: Frederick K. Glick, Esq.

B. Kim Lilly

ATTACHMENT No. 4 to Resolution No. _____

MORRISON | FOERSTER

12531 HIGH BLUFF DRIVE
SUITE 100
SAN DIEGO, CALIFORNIA
92130-2040

TELEPHONE: 858.720.5100
FACSIMILE: 858.720.5125
WWW.MOFO.COM

MORRISON & FOERSTER LLP
NEW YORK, SAN FRANCISCO,
LOS ANGELES, PALO ALTO,
SAN DIEGO, WASHINGTON, D.C.

NORTHERN VIRGINIA,
ORANGE COUNTY, DENVER,
SACRAMENTO, WALNUT CREEK

TOKYO, LONDON, BEIJING,
SHANGHAI, HONG KONG,
SINGAPORE, BRUSSELS

September 11, 2008

Writer's Direct Contact
858.720.7932
WOConnor@mofo.com

Via E-Mail and U.S. Mail

Iris P. Yang, Esq.
McDonough Holland & Allen PC
555 Capitol Mall, 9th Floor
Sacramento, CA 95814-4692

Re: Kim Lilly - Subleases at Paso Robles Airport

Dear Ms. Yang:

We discovered an error in one of the comparable rental rates submitted to the City on August 18, 2008. The Hayward Executive Airport rate of 21.4 cents per square foot per month is incorrect. The correct rate is 21.4 cents per year.

We understand that this developer uses a different approach to this development than Mr. Lilly. Tenants are charged a much higher price for the hangar in exchange for the developer passing on his wholesale ground rent rate to the purchaser of the hangar. The current price for the latest Phase II of closed sales is \$240 per square foot. This would reflect a sales price of **\$600,000** for a Port-A-Port 50' X 50' hangar. The different approaches available to master tenants for setting rates demonstrate the difficulty in using comparables as a basis to set rental rates.

We look forward to hearing from the City regarding Mr. Lilly's request for consent to the proposed rental rates.

Very truly yours,



William V. O'Connor

cc: B. Kim Lilly
Frederick K. Glick, Esq.
John P. Milligan

ATTACHMENT No. 5 to Resolution No. _____

RECEIVED

OCT 10 2008

MORRISON & FOERSTER LLP
SAN DIEGO

Mullen & Henzell L.L.P.

ATTORNEYS AT LAW



e-mail: glyons@mullenlaw.com

October 8, 2008

J. ROBERT ANDREWS
JAY L. BECKERMAN
JOSEPH F. GREEN
MARK S. STATHIS
GREGORY F. FAUERNER
EDWARD C. THOMAS
WILLIAM E. DEGEN
MICHAEL E. GAGE
LORI A. LEWIS
PAUL K. WILCOX
JARED M. KATZ
MONICA M. ROBERTS-MUZNICH
RAMON R. GUERRA
RAFAEL GUINZAUX
JAMA S. JOHNSTON
REBECCA O. BERLMAN
KARLA R. JUNGWIRTH
LINDSAY G. SHANN

Re: Paso Robles Airport – Sublease Matters

Dear Ms. Yang:

Thank you for providing me with a copy of Mr. William O'Connor's letter to you dated August 18, 2008, regarding his client's proposed subleases under the master lease held by the City of Paso Robles ("Master Lease") at the Paso Robles Airport. While I do not make a habit of responding to letters not addressed to me, I find it necessary to correct many of the misstatements contained both in Mr. O'Connor's letter and the letter from Mr. Milligan, which is attached to Mr. O'Connor's letter. We trust the City will take our comments into consideration in its review of Mr. O'Connor's request to approve the proposed subleases at Paso Robles Airport.

I. The Proposed Subleases Fail to Meet the Requirements of the Master Lease and Have Been Rejected by the City and the Majority of Subtenants .

Mr. O'Connor requests that the City consent to eight subleases entered into by his client, Mr. Lilly, at the Paso Robles Airport. Pursuant to the Master Lease, Mr. Lilly, as the Lessee, must receive the City's consent prior to entering into any subleases of property controlled by the Master Lease. We do not believe the City can consent to the proposed subleases because (a) several issues previously raised by the City remain unresolved in the proposed subleases, and (b) the proposed rental rate violates the Master Lease, applicable FAA regulations, and is not supported by any rent rates charged at similar airports. This should not come as a surprise to Mr. Lilly as the City already rejected this exact form of sublease on at least two prior occasions.

Furthermore, the City should not consent to the eight subleases because they represent only a small fraction of the subleases held by Mr. Lilly. As noted by the City in earlier correspondence, Mr. Lilly has failed to receive the City's consent for any of his non-commercial subleases at the Paso Robles Airport. As a result, all of



Iris P. Yang, Esq.
McDonough, Holland & Allen PC
Sacramento, CA 95814-4692
October 8, 2008

Page 2

Mr. Lilly's non-commercial subleases violate the Master Lease. Instead of addressing all of the subleases and corresponding violations of the Master Lease, Mr. Lilly is asking the City to ignore the majority of subleases and to approve a few "favorable" subleases. By presenting only a few subleases to the City, the majority of subtenants are effectively squeezed out of the negotiation process. Mr. O'Connor acknowledges that his client plans to receive the City's approval for the eight subleases, and then force the remaining subtenants to accept the sublease allegedly agreed to "at arms length" by a small minority of subtenants. Mr. Lilly is attempting to use the City's consent to strong arm all the subtenants to accept a sublease they have repeatedly rejected as patently unfair.

Mr. O'Connor suggests that if Mr. Lilly's subtenants don't like the proposed sublease, they should pick up their hangars and find another ground space. The problem with this suggestion is two-fold. First, it wholly ignores the fact that Paso Robles Airport, unlike a private land holding, is public property and subject to specific federal mandates that protect and benefit members of the general public. If Mr. Lilly wants the unfettered ability to charge his subtenants whatever he wants, he should give up his lease at the Paso Robles Airport. Mr. Lilly also fails to acknowledge that because the airport is public property, he is able to lease airport property from the City at a ridiculously low rate. We would encourage the City to consider the profit margin Mr. Lilly would achieve if he were permitted to charge his subtenants 17.5 cents per square foot in light of the rent he pays to the City for the same property, which we understand is less than 1 cent per square foot.

Second, it assumes that the subtenants can simply move their hangars to another location. All of Mr. Lilly's subtenants own their hangars. Many of the subtenants have invested thousands of dollars in large hangars that cannot be relocated. Mr. Lilly is well aware of this fact since he sold many of the subtenants their hangars, at a sizable profit. If Mr. Lilly refuses to renew the subleases, many of the subtenants will lose their hangars.

Mr. Lilly has put his subtenants in a very difficult situation – accept a patently unreasonable sublease or be forced to lose their existing hangars and purchase a new hangar at another location. Clearly, there is much more at stake than a few dollars per month in rent – Mr. Lilly's subtenants are facing a significant economic loss if the City does not enforce the terms of the Master Lease and require Mr. Lilly offer his subtenants a fair and reasonable sublease.



Iris P. Yang, Esq.
McDonough, Holland & Allen PC
Sacramento, CA 95814-4692
October 8, 2008
Page 3

2. Proposed Rental Rate.

Attached to Mr. O'Connor's letter is a letter from Mr. John Milligan. Mr. Milligan states that he worked for the FAA as a civil engineer.¹ According to Mr. Milligan, he has been asked by Mr. Lilly to provide information to the City to "prove" that the proposed rates are in compliance with FAA requirements." Mr. Milligan provides information from a number of airports across California that he considers "comparable to Paso Robles Airport." Mr. Milligan concludes that "the representatives of the subtenants have not provided evidence that the proposed rates offered by Mr. Lilly are unfair or unreasonable."

Mr. Milligan correctly points out that the City must ensure the rent rates charged at the Paso Robles Airport meet FAA requirements and the terms of the Master Lease. As Mr. Milligan states, "it is prudent for a sponsor, as the City has with Mr. Kim's lease, to require its master tenants to gain sponsor approval for lease and rental rates so that the sponsor holds control of rates on its airport." This is a significant shift in Mr. Lilly's position, which up to this point has been that the City has no right to interfere with his sublease negotiations. While Mr. Milligan concedes that the City must control rent rates, he suggests that the City must accept Mr. Lilly's proposed rate unless the City can prove that the proposed rates are unfair and unreasonable. Mr. Milligan improperly shifts the burden of proof to the City. It is the City, not Mr. Lilly, which is the Master Lessor and "airport sponsor". As such, it is the City, not Mr. Lilly, which is ultimately responsible for ensuring the reasonableness of the rent charged at the Paso Robles Airport. We do not believe Mr. Lilly, who is fundamentally motivated to maximize profits, is more qualified than the City, which is ultimately responsible for the operation of the Paso Robles Airport, to determine the appropriate criteria for setting rental rates at Paso Robles Airport. Mr. Lilly has an affirmative obligation to demonstrate that the proposed rental rate meets the requirements of the Master Lease.

3. Mr. Lilly's Continued Failure to Apply the City's Criteria.

The City has repeatedly provided to Mr. Lilly and his counsel the criteria to determine if a proposed rent rate meets the applicable FAA requirements and the

¹ Mr. O'Connor represents that Mr. Milligan is an "expert" in matters related to rate-setting and FAA compliance. We do not believe Mr. Milligan's work as a civil engineer at the FAA has any relevance to the issues at hand, and therefore, we do not consider Mr. Milligan an expert in the matters raised in his letter.



Iris P. Yang, Esq.
McDonough, Holland & Allen PC
Sacramento, CA 95814-4692
October 8, 2008
Page 4

Master Lease. (See Correspondence from Ms. Williamson to Mr. Glick, dated September 19, 2007, December 11, 2007, and February 7, 2008; See Correspondence from Ms. Yang to Mr. O'Connor dated April 7, 2008). The City's criteria are consistent with the plain language and purpose of the FAA policies and Master Lease, and have been affirmed by the responsible FAA representative.

The City has repeatedly asked Mr. Lilly to provide evidence that the proposed rental rate is similar to rates being charged at the Paso Robles Airport and other airports with similar services, facilities and activity levels, and within similar market areas, including airports within a one-hour/sixty-mile commute radius.

Instead of responding to the City's criteria, Mr. Milligan attempts to compare Mr. Lilly's subleases at Paso Robles Airport with leases at airports in Chino, Bakersfield, and Riverside. These airports do not meet the City's criteria. In fact, all three airports were presented last year to the City by Mr. Glick, Mr. Lilly's former attorney, as "comparables" and were flatly rejected by the City. (See Letter from Mr. Glick to Ms. Williamson dated November 1, 2007, and Ms. Williamson's response to Mr. Glick dated December 11, 2007). The City should again reject these comparables, as they do not meet the City's criteria.

Mr. Milligan also provides a chart attempting to compare Mr. Lilly's proposed rental rate with numerous airports throughout California. The City has already rejected several of the airports listed in Mr. Milligan's chart because they do not meet the City's criteria. The remaining airports cited by Mr. Milligan are outside the geographic vicinity of Paso Robles and do not provide the same level of service, facilities or activity levels as Paso Robles Airport. For example, Mr. Milligan cites Van Nuys Airport and Montgomery Field as "comparable" airports. Van Nuys Airport is a towered airport and was recently ranked as one of the "world's busiest airports," averaging 400,000 takeoffs and landings per year. Montgomery Field is a towered airport centrally located near downtown San Diego, California's second largest city, and is home base to approximately 600 aircraft. Paso Robles Airport is a non-towered airport servicing the City of Paso Robles (population 29,500) and is home base to less than 200 aircraft. Mr. Milligan is comparing apples to oranges. The airports cited by Mr. Milligan bear no resemblance to Paso Robles Airport, and therefore, provide no meaningful data to analyze Mr. Lilly's proposed rent rate.



Iris P. Yang, Esq.
McDonough, Holland & Allen PC
Sacramento, CA 95814-4692
October 8, 2008
Page 5

If correctly applied, the City's criteria ensure that any "comparable" airport has certain basic commonalities with Paso Robles Airport. In other words, the City's criteria ensure that everyone is comparing apples to apples. The City should not rely on Mr. Milligan's analysis as it fails to use the required criteria, relies on airports that the City has already rejected, and does not provide an accurate representation of comparable rental rates.

Even if the City were to consider Mr. Milligan's analysis of comparable airports, the majority of the rent rates provided by Mr. Milligan are wrong. We contacted every person listed on Mr. Milligan's chart to confirm the cited rental rate. In nearly every instance, the rent rate provided on Mr. Milligan's chart was substantially higher than the actual rent being charged. We have attached as Exhibit A, a chart comparing the rental rates previously provided by Mr. Milligan and the rates quoted to Mr. Mark Ames. Mr. Ames personally contracted each person listed on Exhibit A during the month of September, 2008. We have also attached a Declaration signed by Mr. Ames affirming the facts provided in Exhibit A.

The only airport cited by Mr. Milligan that meets the City's criteria is San Luis Obispo. You will note that Mr. Milligan's quoted rate of 7 cents per square foot per month at San Luis Obispo is less than half the rental rate proposed by Mr. Lilly. Furthermore, as noted in Exhibit A, the 7 cents per square foot charged at San Luis Obispo reflects more than just ground rent—it also includes association dues that pay for insurance, utilities and other improvements not provided by Mr. Lilly.

While we strongly believe that all of the airports cited by Mr. Milligan (other than San Luis Obispo) have no relevance to the rental rates at Paso Robles and should not be considered by the City as comparable rental values, it is important to correct the information previously provided to the City.

4. City's Criteria for Determining Rental Rate.

Because Mr. Lilly has failed to provide the City with any relevant comparables, we provide the following list of airports and current rental rates. The airports and rates described below meet the City's criteria, as confirmed by the appropriate FAA representative.



Iris P. Yang, Esq.
McDonough, Holland & Allen PC
Sacramento, CA 95814-4692
October 8, 2008
Page 6

a. **Rates Charged at Paso Robles Airport.**

The most relevant rental rates are found at the Paso Robles Airport. Rates at Paso Robles Airport have been reviewed and approved by the City and accurately reflect what is a “fair and reasonable” rental rate. Exhibit B lists what we believe to be all of the rental rates currently charged by Master Tenants, including Mr. Lilly, under subleases approved by the City of Paso Robles. You will note that Mr. Lilly’s proposed rental rate of 17.5 cents per square foot for non-commercial space far exceeds any approved rental rate at the Paso Robles Airport.

Furthermore, Mr. Lilly’s proposed rental rate for non-commercial space is 5.5 cents per square foot higher than the rate he charges for commercial rental space. Mr. Lilly cannot claim that 17.5 cents per square foot is “fair and reasonable” for non-commercial space, when his rate for commercial space is significantly less than 17.5 cents. Based on this fact alone, the City should reject Mr. Lilly’s proposed rental rate.

Based on the rates charged at Paso Robles Airport, which we believe are the most relevant comparables, the “fair and reasonable” rental rate for the ground leased by Mr. Lilly is 5.27 cents per square foot.

b. **Rates Charged by Comparable Airports.**

While the approved rental rates at Paso Robles Airport are the most accurate comparables, they are supported by the additional airports identified by the City within the geographic vicinity of Paso Robles. Provided in Exhibit C are current rental rates for ground leases at San Luis Obispo, King City, and Santa Maria². The average rent rate at these airports for a similar ground lease is 4.76 cents per square foot. This is lower than the current rates at Paso Robles, but exponentially lower than Mr. Lilly’s proposed rate of 17.5 cents. A review of these airports confirms that (a) Paso Robles rent rates are slightly high, but generally in line with comparable airports in the vicinity, and (b) Mr. Lilly’s proposed rent rates and the “comparables” provided by Mr. Milligan are extremely out of line with the comparable rental market for Paso Robles.

² We requested information from Oceano, however, the airport is in the process of evaluating its lease program and could not provide any information on current lease rates.



Iris P. Yang, Esq.
McDonough, Holland & Allen PC
Sacramento, CA 95814-4692
October 8, 2008
Page 7

Conclusion.

Mr. Lilly has had more than a year to resolve his default of the Master Lease. The City and the subtenants directly affected by Mr. Lilly's default have patiently waited for a meaningful response from Mr. Lilly. Instead, Mr. Lilly has provided the City with the same sublease proposal he provided a year ago. Mr. Lilly has repeatedly ignored the City's demands for supporting documentation and refuses to negotiate in good faith with the majority of his subtenants. It is clear to us that Mr. Lilly has no intention of complying with the Master Lease and FAA regulations. Thus, we respectfully request that the City reject the eight proposed subleases. Based on the City's own criteria, we further request that the City direct Mr. Lilly that a rental rate within the average range of those charged at Paso Robles Airport, and the surrounding comparable airports satisfies the terms and conditions of the Master Lease. Without such a definitive statement from the City, we do not believe this matter can be resolved amongst the parties.

Very truly yours,

A handwritten signature in black ink, appearing to read "Graham M. Lyons".

Graham M. Lyons of
Mullen & Henzell L.L.P.

GML:mp

Enclosures

Mr. William O'Connor, Esq.
Clients
G:\19468\0001\CORRO\CR8988.DOC

Declaration of Mark Adams

DECLARATION OF MARK AMES

I hereby declare as follows:

1. I, Mark Ames, am over 18 years of age and competent to make this declaration. I have personal knowledge of the facts stated below and I hereby declare as follows:
 2. My name is Mark Ames.
 3. I have reviewed that certain letter from Mr. William V. O'Connor to Ms. Iris P. Yang, dated August 18, 2008. I have also reviewed that certain letter from Mr. John Milligan to Mr. O'Connor, which letter is attached to Mr. O'Connor's letter to Ms. Yang, including that certain page of Mr. Milligan's letter entitled "Survey of airport ground lease/hangar ownership" ("Survey").
 3. During the period of September 4, 2008 through September 30, 2008, I personally contacted or attempted to contact every person listed in the Survey under that certain heading "Contact" at the telephone number listed in the Survey under that certain heading "Phone #".
 4. In addition to the individuals listed in the Survey, I also contacted other individuals I believed may have knowledge regarding the rental rates charged at those airports listed in the Survey under that certain heading "Location".
 5. During each telephone interview with those individuals listed on the Survey and those individuals listed under the heading "Contact" on the attached Exhibit "A", I asked each individual if he or she was able to provide or had knowledge of the current rental rate for ground space at the particular airport listed under the heading "Location" on the Survey corresponding to that individual's name.

6. During each telephone interview with those individuals listed on Exhibit "A" under the heading "Contact", I took handwritten notes to contemporaneously document my conversation with each individual.

7. I have reviewed the information provided in the attached Exhibit "A" and my handwritten notes taken at the time of each telephone interview, and the information provided in the attached Exhibit "A" accurately describes and reflects the results of my telephone interviews with those individuals listed therein.

I declare that the foregoing is true and correct, and that this declaration was executed this 7th of October, 2008 at Paso Robles, California.


Mark Ames

GA1946840001DOCS\CU7364.DOC

Exhibit A

EXHIBIT A

Survey of Airport Ground Leases

<u>Location</u>	<u>Contact</u>	<u>Phone #</u>	<u>Rental Rate per month/ per square foot Provided by Listed Contact as of September 2008.</u>	<u>Rental Rate Per month/ per square foot Provided by Mr. Milligan</u>
Apple Valley Airport (KAPV)	Ans Scott ¹ /Midfield Aviation	(760) 247-5766	9 cents ²	12.5 cents
Meadows Field (KBFL)	Wink Cecil	(661) 391-4906	3.8 cents ³	15 cents
Chino Airport	Tom Ricotta ⁴	(619) 987-6656	N/A	17 cents
Buchanan Field/Concord	Beth Lee ⁵	(925) 646-5722	3.9 cents ⁶	10.8 cents
El Cajon Airport	Cindy	(619) 562-3040	8.5 cents	19 cents
Hayward Air Terminal	Gary Briggs	(925) 200-0247	2.75 cents ⁷	21.4 cents ⁸
Fox Field/Lancaster (KWJF)	Steve Erving	(661) 940-1709	13 to 14.4 cents ⁹	16.25 cents
Van Nuys Airport	Bob Finkel	(818) 705-9861	30 cents	30 cents
Hawthorne Airport ¹⁰	Bruce McCall	(310) 676-4673	20 cents	26 cents ¹¹
Mammoth Lakes	Pat Foster	(760) 924-9127	15 cents ¹²	16.75 cents ¹³
Riverside Municipal	Sharon	(805) 544-2450	20 cents	20 cents ¹⁴
Montgomery Field	Kevin O'Donnell ¹⁵	(858) 277-1453	N/A	14.4 cents
Palomar Airport ¹⁶	N/A	N/A	N/A	21 cents
Brown Field/ San Diego ¹⁷	Tom Ricotta	(619) 987-6656	N/A	19 cents
San Luis Obispo Airport (KSBD)	Linda Bulter ¹⁸	N/A	N/A	7 cents ¹⁹

Thermal Airport	Ann Goodwin ²⁰	(760) 399-4300	6 cents ²¹	12 cents
-----------------	---------------------------	----------------	-----------------------	----------

GAI9468\0001\DOCSCT9262.DOC

¹ Mr. Milligan did not provide a contact number for "Joe" on his chart. Ans Scott operates Midfield Aviation, which rents 54 ground spaces with 1,100 square foot hangars at \$100/mo.

² Apple Valley Airport has extremely limited ground space. There is a waiting list of 76 people for ground space. Paso Robles Airport does not have these constraints, and in fact has more ground space than is currently used.

³ Meadows Field charges a flat rate of \$65 per month for ground space, which can accommodate up to 1,700 square feet of hangar space. Subtenants also receive a 10% discount on their rent if they prepay for the entire year. The 3.8 cents reflects a 1,700 square foot hangar @ \$65 per month (excluding the 10% "prepay" discount).

⁴ Mr. Ricotta would not verify the rent rate for this airport.

⁵ Mr. Milligan's chart references "Julie" as the contact; however, when Mr. Ames contacted Julie, she referred him to Beth Lee, who is responsible for rentals at Buchanan.

⁶ Ms. Lee's company subleases 143,850 square feet of ground space for a total amount of \$5,607.42, which equals 3.9 cents per square foot, per month.

⁷ Hayward is similar to Mr. Lilly's subleases in that Mr. Briggs sold his subtenants their hangars and now rents them the ground space. However, unlike Mr. Lilly, Mr. Briggs has reduced his rental rate to reflect the fact that he has already made a significant profit from the initial sale of the hangars.

⁸ Mr. Milligan did not provide a "current rate rent", but did provide a "proposed rent rate."

⁹ Ground space rents for \$130 per month and can accommodate a hangar of 900 to 1,000 square feet.

¹⁰ Mr. Milligan provided no contact information, and therefore, the rent rate he provided cannot be verified. However, we contacted Bruce McCall, whose company Million Air, is in the process of building box hangars at Hawthorne Airport. Mr. McCall believes the ground rent for these new box hangars will be approximately 20 cents per square foot.

¹¹ Mr. Milligan did not provide a "current rate rent", but did provide a "proposed rent rate."

¹² Given the remote location and resort destination associated with Mammoth Lakes, ground space at this airport is extremely limited.

¹³ Mr. Milligan did not provide a "current rate rent", but did provide a "proposed rent rate."

¹⁴ Note that Mr. Lilly and his business partner/attorney control the leases at Riverside Airport and the rates quoted are their own rental rates.

¹⁵ Mr. O'Donnell declined to speak to Mr. Ames regarding the rents charged.

¹⁶ Mr. Milligan provided no contact information, therefore, the rent rate he provided cannot be verified.

¹⁷ Mr. Ricotta would not verify the rent rate for this airport.

¹⁸ Mr. Milligan provided no contact information, however we contacted Ms. Butler, who is a member of the SLOCAHOA, one of the hangar associations at KSBP.

¹⁹ Mr. Milligan provides no contact information for this comparable, so we cannot confirm its accuracy. However, in contacting several lessees at KSBP, we are confident that the 7 cents rate reflects the amount hangar owners pay to their Association, which then pays rent to the County. The County charges a ground rent rate of 1.3 cents per square foot, with the remainder of the rent amount charged by the Association going to improvements for the benefit of the hangar owners (i.e. electricity, plumbing, insurance). None of the benefits provided by the Association are provided by Mr. Lilly, and therefore the 7 cents is not an accurate comparable.

²⁰ Mr. Milligan listed Penny Nelson as his contact. Ann Goodwin is Penny Nelson's business partner.

²¹ Ms. Nelson's and Ms. Goodwin's operation controls the ground space for 22,000 square feet of hangar space for which they charge \$950 per month in ground rent. In addition, the subtenants are required to pay additional rent for use of certain common use areas. The total ground rent (hangar space plus common use area), is 6 cents per square foot/per month.

Exhibit B

EXHIBIT B

Paso Robles Airport Hangar Group Comparable Ground Rental Rates

Rental Rates at Paso Robles Airport Approved by the City of Paso Robles

Name of Master Tenant: Kim Lilly

Name of Subtenant: Marguerite Nunn

Size of Ground Space: Approximately 4,300 square feet

Permitted Uses: Commercial Hangar

Infrastructure Provided: Electricity, plumbing

Rent per square foot, per month: 12 cents (based on original rent rate approved in 2003, as adjusted by permitted CPI increases).

Name of Master Tenant: Nunno Corporation

Size of Ground Space: 1,800 square feet

Permitted Uses: Non-Commercial

Rent per square foot, per month: 5.27 cents

Nunno Corporation operates a nearly identical business as Mr. Lilly, in that it holds a Master Lease with the City and rents out ground space to subtenants, who own the overlying improvements.

Exhibit C

EXHIBIT C

Paso Robles Airport Hangars Comparable Ground Rental Rates

Criteria Used for Comparables:

Airports within Sixty Miles and/or One Hour Travel Time of Paso Robles Airport
(Per City's Criteria in its December 11, 2007 Letter to Mr. Glick)

Name of Airport: King City (KIC)

Mark Plaskett (831) 385-5956

Mr. Plaskett rents 1,400 square feet of ground space for his privately-owned hangar at a rate of \$78 per month.
(5.57 cents/sq.ft/mo.)

Name of Airport: San Luis Obispo (SBP) I.

Phil D'Acri (805) 781-5218

Airport has both County-owned hangars and ground leases for privately-owned hangars. For the privately owned hangars, the ground is leased to a group/association, which then subleases individual hangar spaces to its members. The ground rent runs in a range from 50 cents/sq.ft/yr (4.16 cents/sq.ft/mo.) to 55 cents/sq.ft/yr. (4.58 cents/sq.ft./mo.)

No land available at this time for development of new hangars.

San Luis Obispo (SBP) 2.

Private Hangar Association. (Hangar 46)

Mike Kunde (805) 215-8914

Association has a long term lease (ten years remaining on the current term) with the airport.

The tenants are members of the association.

Each tenant pays the association a quarterly fee, which includes ground rent, as well as maintenance fees for the taxi-ways and landscaping.

The fee is 7.8/sq.ft/mo.

ATTACHMENT No. 6 to Resolution No. _____

MORRISON

| FOERSTER

12531 HIGH BLUFF DRIVE
SUITE 100
SAN DIEGO, CALIFORNIA
92130-2040

TELEPHONE: 858.720.5100
FACSIMILE: 858.720.5125
WWW.MOFO.COM

MORRISON & FOERSTER LLP
NEW YORK, SAN FRANCISCO,
LOS ANGELES, PALO ALTO,
SAN DIEGO, WASHINGTON, D.C.
NORTHERN VIRGINIA,
ORANGE COUNTY, DENVER,
SACRAMENTO, WALNUT CREEK
TOKYO, LONDON, BEIJING,
SHANGHAI, HONG KONG,
SINGAPORE, BRUSSELS

October 24, 2008

Writer's Direct Contact
858.720.7932
WOConnor@mofo.com

Via E-Mail and U.S. Mail

Iris P. Yang, Esq.
McDonough Holland & Allen PC
555 Capitol Mall, 9th Floor
Sacramento, CA 95814-4692

Re: Kim Lilly - Subleases at Paso Robles Airport

Dear Ms. Yang:

This responds to the October 8, 2008 letter from Mr. Lyons regarding Mr. Lilly's request that the City consent to twelve subleases.¹ The purpose of Mr. Lyons' letter is self-explanatory, but most troubling is the conclusion requesting "that the City *direct* Mr. Lilly that a rental rate within the average range of those charged at Paso Robles Airport, and the surrounding comparable airports satisfies the terms and conditions of the Master Lease." (Letter from G. Lyons to I. Yang dated October 8, 2008 at 7.) This pronouncement goes against the City's repeated refrain that "the City has no authority or desire to set lease rates for subleases at the Paso Robles Airport." (Letter from I. Yang to W. O'Connor dated April 7, 2008 at 2.) Mr. Lyons' position, and presumably that of his clients, crystallizes the fundamental problem with the City's approach to the subleasing issue under Section III of the Master Lease. Mr. Lilly has provided ample documentation showing that the proposed rental rate satisfies the Final Policy Regarding Airport Rates and Chargers ("FAA Policy") and that the City has implemented an unprecedented process to obtain consent to subleases under the Master Lease.²

¹ The following leases have been submitted to the City for approval: Pete Johnson Chevrolet, Hastings Ranch Vineyard, Eberle Winery, Chris Henry, William Hurst, Jim Judd, Hogue Bros., Inc., Black Oaks, Inc., and four leases relating to Aero Services and John Moore. These subtenants have not objected to the rental rate of 17.5 cents per square foot and are not represented by Mr. Lyons.

² Please see my letter of April 1, 2008 which describes in detail the FAA Policy and its application to Mr. Lilly's Master Lease, and Mr. Milligan's August 18, 2008 letter describing the common practice of allowing the master tenant and proposed subtenants to negotiate rates by agreement without interference by the airport sponsor. Further, Mr. Lilly's August 18, 2008 submission establishes that the proposed rental rate complies with FAA Policy and the terms of the Master Lease.

Iris P. Yang, Esq.
October 24, 2008
Page Two

The stated goal of Mr. Lyons' clients—to cause the City to direct Mr. Lilly to set rates according to inappropriate criteria—is a misguided application of FAA Policy and the terms of the Master Lease. I have encouraged the City on prior occasions to consult with FAA airport compliance personnel and review the subleasing issues at Paso Robles Airport. *See* 49 U.S.C § 47129(a)(3) (the FAA Act is not intended to “set the level of the fee”). I must reiterate that request again because it is our view that the FAA would not condone the method in which the City is basing its refusal to consent to the twelve subleases.

It is unreasonable for the City to continue to delay consent based on a flawed analysis of FAA Policy and attempt to further referee a dispute with Mr. Lilly’s subtenants. Moreover, if the City were to ultimately withhold consent based on a flawed analysis of the FAA Policy and the terms of the Master Lease, that action would also amount to an unreasonable refusal to consent to the proposed subleases. Mr. Lilly encourages the City to act quickly and approve the proposed subleases without further delay. If the City refuses to consent to the proposed subleases, Mr. Lilly requests that the City explain its reasons so we can evaluate the reasonableness of its refusal to consent.

Unfortunately, Mr. Lyons’ letter also contains several inaccurate assertions and unnecessary hyperbole regarding the history of the sublease negotiations. Once again we are compelled to respond to the most recent line of attacks from a disgruntled few whose ultimate objective is to drive the rental rate down to a point that does not make long-term economic sense and puts an unrealistic burden on Mr. Lilly to operate his business at rates below the current market. The following is Mr. Lilly’s detailed response.

First, Mr. Lyons claims that “several issues previously raised by the City remain unresolved in the proposed subleases.” (Letter from G. Lyons to I. Yang dated October 8, 2008 at 1.) Presumably, Mr. Lyons is referring to issues regarding the *form* of the proposed sublease, putting aside the rental rate. Since my first telephone call with you and Mr. Lyons, and my recent call with you on October 9, 2008, Mr. Lilly has requested that the City inform him of any issues with the sublease terms. To date, Mr. Lilly has not received a response from the City. Accordingly, this seems to be a “non issue,” as the City has not identified any particular area of concern regarding the form of the proposed sublease aside from the rates. It would be unreasonable at this late stage for the City to identify any such problem now that most of the subleases were submitted for approval over six months ago. (Letter from W. O’Connor to M. Williamson dated April 1, 2008.)

Second, Mr. Lyons mistakenly attempts to characterize Mr. Lilly’s compliance with the City’s requests as strong arm tactics because the twelve subleases “represent only a small fraction of the subleases held by Mr. Lilly” and those subleases appear to be “favorable” to Mr. Lilly. (Letter from G. Lyons to I. Yang dated October 8, 2008 at 2.) Putting aside the inaccuracy of this statement, Mr. Lyons’ letter acknowledges that his clients’ subleases are not before the City for consent. It defies logic that non-signatories to the proposed subleases

Iris P. Yang, Esq.
October 24, 2008
Page Three

may object to its terms, including the rental rate. Indeed, the FAA Policy explicitly precludes such a result. *See* FAA Policy, 61 Fed. Reg. 31, 994 (June 21, 1996) (in keeping with the policy to encourage direct local negotiations, the FAA does not look favorably on complaints regarding fees set by agreement lodged by non parties). No doubt the City understands that there is a fundamental standing issue here. Thus, the City must be cautious when considering the source of the complaints about the proposed rental rate. To refuse consent to the proposed subleases based on the comments of non-signatories is unreasonable.

It is also inaccurate to suggest that the subleases currently before the City represent only a “small fraction” of Mr. Lilly’s subtenants. The opposite is true. There are 46 hangar spaces on Mr. Lilly’s leasehold. Of the 46 hangar spaces, Mr. Lilly owns seven hangars, or 14.6% of available hangar spaces. There are 13 hangar spaces that have City-approved subleases or have executed subleases presently before the City for consent (this includes the eight subleases of individuals who are not represented by Mr. Lyons). This group of 13 represents 27% of the hangar spaces. There are six additional hangar spaces occupied by tenants who are not represented by Mr. Lyons and have not signed a new sublease. This group consists of 12.5% of the hangar sites. Some of these subtenants have indicated that they intend to sign new subleases once the deadlock is broken regarding the proposed rental rate. Five of Mr. Lyons’ clients previously signed subleases, but now complain that the sublease was obtained under duress.³ This faction represents 10.4% of the hangar spaces. Finally, there are 15 hangar sites whose current tenants do not have a signed lease and are represented by Mr. Lyons. This final group represents 31.5% of the hangar sites.

The percentage breakdown of the various hangar sites does not support the assertion that “only a small fraction” of subtenants have no objection to the proposed rental rate. Indeed, more than half of the tenants, as represented by the number of hangar sites, have no objection to the proposed rate. Assuming for the moment that Mr. Lyons’ concept of majority rule is proper, the City cannot withhold consent to the proposed subleases because, in reality, it is a minority of subtenants, many of whom are holdover tenants, that continue to obstruct efforts by Mr. Lilly and willing subtenants to conclude long term subleases.

Third, Mr. Lyons takes issue with Mr. Milligan’s observation that “the City could now undertake its option to provide other space on the airport for a subtenant, who is unable to arrange satisfactory terms with Mr. Lilly, to relocate elsewhere on the airport at his own expense, assuming such space is available.” (Letter from J. Milligan to W. O’Connor dated

³ The claim of “duress” by some of Mr. Lyons’ clients is disingenuous. The FAA Policy does not condone this gamesmanship and expressly provides the FAA will not allow airport users to improve upon their bargaining position by bringing an affirmative complaint after an agreement has been reached; this outcome is unfair to airport proprietors who bargain in good faith. *See* FAA Policy, 61 Fed. Reg. 31, 994 (June 21, 1996). Moreover, the FAA will not consider complaints about fees set by agreement if filed by parties to the agreement. *Id.*

Iris P. Yang, Esq.
October 24, 2008
Page Four

August 18, 2008 at 4.) Mr. Lyons complains that this option is problematic because (i) Mr. Lilly must operate his leasehold for the benefit of the general public, and (ii) many of the subtenants have hangars that cannot be relocated. (Letter from G. Lyons to I. Yang dated October 8, 2008 at 2.)

To suggest that Mr. Lilly has an obligation to the public-at-large to make hangar sites available to subtenants on terms that make no economic sense is an unstudied analysis of the varied considerations and policies regarding airport rates and charges. It is true that the City, as airport sponsor, does have the obligation to comply with various FAA Grant Assurances in exchange for accepting funds under the federal Airport Improvement Program. (Letter from J. Milligan to W. O'Connor dated August 18, 2008 at 2.) It has been previously demonstrated, however, that the proposed rate complies with FAA Policy and it should go without saying that the rate takes into account various cost components including maintenance, insurance, property tax, state income tax, federal income tax, and estate tax. See FAA Policy 61 Fed. Reg. 31, 994 (June 21, 1996) (a reasonable rate includes all operating and maintenance expenses directly associated with the provision of airfield aeronautical services, including all capital costs associated with the provisions of such services currently in use, and current costs of planning future aeronautical facilities and services). The public interest in well run airport facilities is "best accomplished by profit motivated private enterprise." (Letter from J. Milligan to W. O'Connor dated August 18, 208 at 3.) Mr. Lilly has a right to operate his leasing business in the black and under no circumstance may he be compelled to operate his business at below market rates. FAA Policy, 61 Fed. Reg. 31, 994 (June 21, 1996) (the provision of aeronautical services must be self sustaining). The public cannot be better served by forcing Mr. Lilly to run his business below market rates, which has the potential to dilute the quality of aeronautical services offered at Paso Robles Airport.⁴

Furthermore, the claim that the hangars cannot be relocated is suspect. The hangars are all Port-A-Port hangars that may be relocated to other airports or other sites at Paso Robles Airport should the City choose to make the land available. The larger box hangars and large common-wall "T" style hangars can be moved because Mr. Lilly himself has moved several hangars successfully in the past. Mr. Lyons' clients desire to continue to enjoy the service offered by Mr. Lilly on his leasehold, but do not want to pay market rates for that service. The possibility of having to move a hangar should come as no surprise to any subtenant, and to withhold consent to the proposed subleases on this consideration is unreasonable.

Fourth, Mr. Lyons takes issue with Mr. Milligan's main premise that it is improper for an airport sponsor, such as the City, to expect "a master tenant to 'prove' that proposed rates are

⁴ Mr. Lilly has been a long-term friend of the private pilot and has worked tirelessly to promote a pilot's right to own his own hangar. Moreover, Mr. Lilly has made a significant investment in the quality of service at Paso Robles Airport which has benefited his tenants and the City over the years.

Iris P. Yang, Esq.
October 24, 2008
Page Five

comparable to like kind arrangements as the City has demanded of Mr. Lilly.”⁵ (Letter from J. Milligan to W. O’Connor dated August 18, 2008 at 4.) Mr. Lyons continues to argue, without any support, that the onus is on Mr. Lilly to “prove up” his proposed sublease rate. Mr. Milligan conclusively demonstrated that this process is not endorsed by the FAA Policy. Mr. Lilly refuses to continue to bow to the unsupported assertions and recurring misunderstandings of FAA Policy regarding rates and charges. If this matter were to progress further, Mr. Lilly is confident that the burdens of the respective parties have been correctly defined in our submissions. The City’s refusal to consent to the proposed subleases according to its own concept of the applicable burdens of proof is therefore unreasonable.

Fifth, Mr. Lyons suggests that Mr. Lilly’s August 18, 2008 submission failed to apply the City’s criteria for using comparable rates to establish the proposed sublease rate is fair and reasonable. As a preliminary matter, Mr. Lilly does not agree that the use of comparable rates is dispositive of whether a proposed rate or charge is fair and reasonable. That position has been well documented in my letters to the City and John Milligan’s August 18, 2008 letter. As I have discussed with you, the City can engage in an endless three-way debate over which rates are comparable or not. What we think are apples and oranges, Mr. Lyons will claim are apples and apples—and on and on we go. The history of this dispute clearly demonstrates the problems associated with using comparables as the sole basis to set rental rates.

Perhaps most disconcerting is Mr. Lyons’ inaccurate attempt to define an arbitrary geographic limitation for “comparable” rental rates that the City has never endorsed itself. Indeed, the City requested that “Mr. Lilly provide evidence that is reasonably satisfactory to the City that the proposed rental rates for the hangars are comparable to those being charged at other airports with similar facilities and services and/or within similar market areas.” (Letter from I. Yang to W. O’Connor dated July 3, 2008.) The City also clarified that Mr. Lilly’s Master Lease was not in default and acknowledged that Mr. Lilly “may also use other factors as well in developing a counterproposal.” (*Id.*) Mr. Lyons misleadingly defines the City’s criteria to include only those airports within a one-hour/sixty-mile commute radius. To withhold consent to the proposed subleases based on comparables from airports within a one-hour/sixty-mile commute radius is arbitrary, inconsistent with the City’s July 3, 2008 letter, and FAA Policy. Therefore it is unreasonable for the City to only consider comparable rates based on such geographic limitations.

⁵ Mr. Lyons takes an uneducated swipe at Mr. Milligan’s qualifications and implies that Mr. Milligan’s opinions are based only on his experience as a civil engineer. This assertion demonstrates a fundamental misunderstanding of Mr. Milligan’s point in his letter wherein he states that his work with the FAA as Supervisor of the Airport Standards Section of the Airports Office (Los Angeles) included compliance issues regarding an airport sponsors’ obligations under the Grant Assurances and the FAA Airport Improvement Program. Mr. Milligan is highly qualified to offer opinions on the Paso Robles Airport subleasing issue. Again, I encourage the City to contact the FAA to confirm Mr. Milligan’s qualifications based on his 34 years of service with the FAA.

Iris P. Yang, Esq.
October 24, 2008
Page Six

Sixth, Mr. Lyons claims that some of the comparable rental rates submitted to the City on August 18, 2008 are inaccurate. As a threshold matter, it is a difficult exercise to collect completely accurate data from Mr. Lilly's competitors regarding their airport rates and charges. This information is proprietary and businesses are generally hesitant to give it out. This is evidenced by the fact that Mr. Ames was unable to confirm rates that we obtained.⁶ It is unfair to hold these discrepancies against Mr. Lilly when it is the City that insisted that we expend significant time and effort collecting data that may be inherently unreliable. In any case, attached at Tab A to this letter is Mr. Lilly's response to the rate discrepancies identified by Mr. Ames.

Notwithstanding the attached clarification from Mr. Lilly, the rental rates collected by Mr. Ames average out to 12 cents per square foot. Moreover, if one assumes the rates listed as "N/A" are accurately reported in Mr. Lilly's submission, the average rate goes up to 14 cents per square foot according to their own numbers. The rate Mr. Lilly proposes is therefore in the ballpark of comparable rates offered at similar airports in similar markets even if it is assumed that Mr. Ames' analysis is accurate. However, as discussed in more detail at Tab A, Mr. Lilly does not accept this analysis as correct and, taking into account certain clarifications, the average of the rates submitted to the City for consideration is 16 cents per square foot. (See Tab B for corrected rate summary.)

In light of the above, it is not surprising that Mr. Lyons retreats to rates charged at King City Airport, San Luis Obispo, and Santa Maria. Those airports, however, are not comparable to Paso Robles Airport. None of these airports have ground space available under the same lease concept or business model that Mr. Lilly has a Paso Robles Airport. And the rates listed are old lease rates.

Seventh, Mr. Lyons claims that Mr. Lilly's proposed rental rate is 5.5 cents per square foot higher than the rate he charges for commercial rental space relying on Marguerite Nunn's sublease. That assertion is misleading. Mrs. Nunn's sublease commenced in 2003 at \$550 per month for a 4,180 square foot hangar (not 4,300 square feet as Mr. Lyons claims) for an effective rate of 13.16 cents per square foot. Moreover, the same size hangar and identical form of lease was approved for Mr. Hogue in 2006 at a rate of 17.9 cents per square foot, representing the fair market rate at that time for a commercial use hangar. The fact that Mr. Hogue and several other subtenants are now willing to pay at least 17.5 cents per square foot for five years in 2008 clearly demonstrates the proposed rate is fair and reasonable.

Eighth, Mr. Lilly takes exception to the suggestion that he has been unwilling to negotiate with the objecting subtenants. This is simply untrue. As early as February of 2008, Mr. Glick, on behalf of Mr. Lilly, offered to mediate the dispute with Mr. Lyons' clients.

⁶ Mr. Lilly submitted rates from 16 different airports. Of these 16 airport locations, Mr. Ames was unable to obtain information from five airport businesses. These five airports are listed as "N/A."

MORRISON | FOERSTER

Iris P. Yang, Esq.
October 24, 2008
Page Seven

(Letter from F. Glick to G. Lyons dated February 7, 2008.) In response to that offer, Mr. Lyons refused mediation as an option. (Letter from G. Lyons to F. Glick dated February 20, 2008, attached at Tab C.) Moreover, the proposals from Mr. Lyons have been complete non starters. For example, in his recent letter and in the past, Mr. Lyons has suggested that the subtenants should pay *less* than they have in the past. These intractable positions are to blame for the current deadlock.

Furthermore, before Mr. Lyons became involved in this dispute, Mr. Lilly personally met with Messrs. Rezich and Cole in August of 2007. They also claimed to negotiate on behalf of several subtenants. The result of that meeting was an agreement to pay 14 cents per square foot. (Letter from K. Lilly to Subtenants dated August 7, 2007 attached at Tab D.) Messrs. Rezich and Cole later backed out of that agreement and resorted to baseless threats from an attorney. *See, e.g.*, Letter from G. Lyons to F. Glick dated January 23, 2008 ("we will file an action against your client" and "seek punitive damages" and "recovery of our legal fees.") This bad faith conduct is squarely rejected in the FAA Policy. *See* footnote 3, *supra*.

Finally, we trust you will discuss this response to Mr. Lyons' October 8, 2008 letter with the City. We have been seeking the City's consent to the subleases for several months now and have not received a substantive response. The City must act on Mr. Lilly's request. If the City refuses to consent to the proposed subleases, it must explain its reasons, as the Master Lease expressly states that such consent will not be unreasonably withheld.

We look forward to hearing from the City regarding Mr. Lilly's request for consent to the proposed rental rates at Paso Robles Airport. We have waited patiently for many months and would appreciate a response as soon as possible.

Very truly yours,



William V. O'Connor

cc: B. Kim Lilly
 Frederick K. Glick, Esq.
 John P. Milligan

Tab A

Recap of Discrepancies of Exhibit A and Mr. Ames' Notes

#1 & #2 Apple Valley - Midfield Aviation – Ans Scott

The correct square foot rate is 9 cents however this is an old rate under Midfield's old lease. New rates this year will be much higher. My 12.5 cents rate was for the small hangar and Midfield has the Executive I size hangar (my error). Mr. Ames has omitted the cost to develop new land at Paso Robles Airport, regarding land availability. Land availability and cost to develop a site is surely a large part of current fair market values.

#3 Meadows Field

Meadows Field was reported incorrectly. After rechecking with Atlantic Aviations, Mr. Wink Cecil, I was informed they charge \$65.00 per month for their small Port-A-Ports ($65 \div 804 \text{ sq. ft.} = 8.1 \text{ cents per sq. ft.}$). Their rates are for month to month on airport tie down ramp space. No development costs were incurred however Atlantic pays the airport for this developed tie down area in their Master Lease. Mr. Cecil will be raising rates in January and will use market rates he has developed. Mr. Cecil pointed out Lloyds Aviation has airport property that they developed for recreation vehicle storage. I called Nancy at Lloyds Aviation and their rates for parking a recreation vehicle is \$195 for a 60' X 12' space ($60 \times 12 = 720 \text{ sq. ft.}$ $\$195.00 \div 720 = 27 \text{ cents per sq. ft.}$) and smaller spaces 40' X 12" for \$65.00 ($65 \div 480 = 13.5 \text{ cents}$). The recreation vehicle storage rates clearly shows why the 40' smaller units take up less driveway space compared to the 60' units, because larger recreational vehicle need larger driveways). This fact also impacts hangars because we have to have to provide a full width taxiway.

#4 Brownfield/Chino

Tom Ricotta owns leases at both Brownfield in San Diego County and Chino Airport in Chino, California. I have enclosed a notice to his tenants as of April 22, 2008 confirming the 19-cent old rate and the new rate of 21 cents. (Exhibit 1)

#5 and #6 Buchanan

Again Mr. Ames is trying to compare airport direct to end user ground rates. The 3.9 cents is the correct rate for an old Port-A-Port hangar project Master Lease. At present a new lease with the tenant and airport for a higher rate is not available. Bare in mind this site is a fully developed parcel and the rates charged to the subtenants is as stated .108 and will go higher under new lease rates now being considered. Also note Mrs. Lee is an employee of Buchanan Field and the figures Mr. Ames states "her company" is a disingenuous comment to make it appear that she has her own company. She confirmed to me the above information that the airport charges the leaseholders.

#7 Hayward

Hayward's figures I have already corrected however again remember at this project the high cost of the hangars off set the at-cost ground rent. I am sure at the end of this current lease, the ground rent will go up to market rates.

#8 Hayward

The .214 per year is the current rate not the proposed rate.

#9 Fox Field?

Again this is the rare case where the airport rents directly to the individual Port-A-Port hangar owner. These rates are for month-to-month. The \$130.00 rate is for the Executive size of 804 square feet up to 1,000 square feet so the variable rate would be 13 cents to 16.2 cents.

#10 and #11 Hawthorne

Hawthorne Airport is again a new project and price of hangars is a factor in ground rates. 26 cents was the rate I received when I called. Hawthorne is a very small airport in a very undesirable area of Los Angeles. This rate is viable because it is Master Lease holder to individual tenants when Master Lease holder has had to do extensive site improvements as I have done.

#12 and #13 Mammoth

Mammoth is another good example of Master Leaser holder to subtenant. Small airport and a resort destination, Paso Robles is much larger, has more population and is likewise a destination location and becoming more so. Mr. Ames' comment about how ground space is limited is not accurate, however "developed" ground space is limited as is in Paso Robles. The rental rate is 16.75. The 15 cents Mr. Ames listed was before the current consumer price index rate increases were added.

#14 Riverside

Riverside is a correct comparison that clearly sets market rates. Airport owner is the County (Master Lessee). Port-A-Port Leasing is a separate partnership that manages the Master Lease separately from any of my business interests. Port-A-Port Leasing subleases to hangar owners subtenants and rates posted by Mr. Milligan are 2-year old rates (i.e. 20 cents).

#15 Montgomery Field

Please find attached copies of the cover sheet of a typical sublease (Exhibit 2) dated in 2002 with the rate posted on page 2 and footage shown on page #1. This rate is 6 years old and the consumer price index clause has brought the rate up to approximately 23.5 cents currently. For further confirmation, please call Mr. Kevin O'Donnell at 858/277-1453.

#16 Palomar Airport (Carlsbad)

This is a County to subtenant association direct lease. Subtenant did not develop site however in getting a new lease a few years ago (about 5 years, I think), the association pooled tenant funds to upgrade the site and agreed to the new rate of 20.6 cents plus consumer price index. To contact the county call Olivia Brackett at the county at 760/495-4938.

#17

See Mr. Ricotta's letter mentioned in #4. Mr. Milligan rates are correct. You may call Mr. Ricotta at 619/987-6656.

#18 & #19 San Luis Obispo

San Luis Obispo is a county to end user agreement with respect to the Port-A-Port hangar on the San Luis Obispo airport. The 7 cents rate is an old rate. No more land is available for Port-A-Port hangars. Other county to hangar association leases with different terms, conditions and start dates are on this airport. Needless to say no current land is available and the rate is too old to be comparable.

Tab A
Exhibit 1

10/17/2008 12:33 FAX 8052389424

07/09/2008 12:46 6196719665

LANCAIR

010
PAGE 01/01

EXHIBIT III



April 22, 2008

Dear Tenants.

In accordance with the letter you were given May 1, 2007 regarding the rental increases, the 12 month increase will take affect May 1, 2008. As stated in the previous letter your current rent is approximately \$.19 per square foot. The new rent will be \$.21 per square foot. Due to economic times we will not be charging the CPI increase at this time as the letter stated. A copy of the 2007 letter has been included for your records.

Best regards,

Tom Ricotta

1424 Continental Street, San Diego, CA 92154
Phone 619-671-9222 * Fax 619-671-9665

Agenda Item 1 Page 76 of 87

FAX
805-238-9924

Tab A
Exhibit 2

EXHIBIT IX

Air 88, Inc. dba: Crownair Aviation
3753 John J. Montgomery Drive
San Diego, CA 92123
Phone 858-277-1453 Fax 858-277-7591

Sublease

Air 88, Inc., d.b.a. Crownair Aviation, a California corporation, herein called "Sublessor", hereby subleases to [REDACTED], herein called "Sublessee", the land for a hangar measuring 7,323 square feet, the construction of which was done only as approved, permitted and certified by the City of San Diego, herein called "City", on land herein called "the Premises", located on all of that certain property situated in the City of San Diego, County of San Diego, State of California, described as Lease Lot 9, Montgomery Field Airport, delineated on Exhibit "A" as described in Subsection 10.1 of City of San Diego Flat Lease. The Premises are shown on the plot map attached hereto as Exhibit B. This Sublease relates specifically to the area shown as Hangar # 35.

Recitals

- A. Sublessor is the lessee under that certain lease dated May 6, 1996 (the "Master Lease") by and between Sublessor and the City of San Diego (the "City"), a copy of which is attached hereto as Exhibit C.
- B. Sublessee has purchased or has contracted to purchase an aircraft hangar (Hangar # 35) on the Premises. Such purchase is contingent on Sublessee obtaining the rights to the Premises under this sublease and the consent of the City to this sublease (as evidenced by a "Consent to Sublease Agreement").

NOW, THEREFORE, the parties agree as follows:

1. **Leasing and Description of Property.** Subject to the terms and conditions set forth herein, Sublessor hereby subleases the Premises to Sublessee, and Sublessee hereby subleases the premises from Sublessor.
2. **Term.**
 - (a) This Sublease shall commence on the date of Transfer of Title and shall end on **May 31, 2016** unless sooner terminated as provided herein. In the event the Master lease is extended, Sublessor will, subject to approval by the City, offer an extension to this sublease for the same duration of any subsequent master lease executed between Sublessor and the City. Such offer, if approved by the City, shall be made prior to termination of the Master Lease. The terms of the extension or new sublease, subject to approval by the City, will be proportional to the rent in this sublease and to the percentage (%) increase to the new or extended master lease.
 - (b) So long as Sublessee is not in default in the performance of any of the terms, covenants, or conditions of the Sublease, City will not join Sublessee as a party defendant in any action or proceeding for the purpose of terminating Sublessee's interest and estate under the Sublease because of any default by Lessee/Sublessor under the Master Lease.

- (c) If the Master Lease is terminated for any reason, all Sublessor's interests as Sublessor under the Sublease shall be deemed automatically assigned, transferred and conveyed to the City. City shall thereafter be bound on the Sublease to the same extent Lessee/Sublessor was bound on the Sublease, and shall have all the rights under the Sublease that Sublessor had under the Sublease. Further, upon such a termination, Sublessee shall be bound to City under all of the conditions of the Sublease for the balance of the term of the Sublease with the same force and effect as if City were the landlord under the Sublease. In no event shall the City be required to approve an extension of the Sublease beyond May 31, 2016. As a part of this process, Sublessee shall attorn to City as Sublessee's landlord. The attornment will become effective immediately when City succeeds to the interest of Sublessor under the Sublease, and shall not require the execution of any additional instruments by the parties to this agreement. The respective rights and obligations of Sublessee and City upon attornment shall for the balance of the term of the Sublease be the same as they are currently set forth in the Sublease, with the exception of the potential extension provision.

Subject to specific exceptions herein, if the Ground Lease is terminated for any reason and City succeeds to the interest of Sublessor under the Sublease, City shall be bound to the Sublessee under the terms of the Sublease, and Sublessee shall, from and after that event, have the same remedies against City for the breach of any agreement contained in the Sublease that Sublessee might have had under the Sublease against the Sublessor.

3. Ground Rent. Sublessee agrees to pay a flat rate of One thousand five hundred twenty-eight Dollars (\$ 1,528.00) per month. Ground rent will begin and be payable on the first (1st) day of the month for the full term of the lease. Ground rent is payable at the office of Sublessor at **Crownair Aviation, 3753 John J. Montgomery Drive, San Diego, CA 92123**, or at such other place or places as Sublessor may from time to time designate by written notice delivered to Sublessee.

4. Ground Rent Adjustment. The ground rent provided for in Section 3 above shall be subject to adjustment at the end of the first year and at the end of every year thereafter (the "adjustment date") based on increases in the Consumer Price Index as follows:

The Base for computing the adjustment is The Consumer Price Index for All Items for All Urban Consumers in the Los Angeles-Riverside-Orange County Metropolitan Area, published by the United States Department of Labor, Bureau of Labor Statistics ("Index"), which is last published prior to the date of the commencement of the term ("Beginning Index"). If the Index published nearest (and prior to) the adjustment date ("Extension Index") has increased over the Beginning Index, the ground rent for the following annual period (until the next rent adjustment) shall be set by multiplying the minimum rent set forth in Section 3 (post flat-rate master lease) above by a fraction, the numerator of which is the Extension Index and the denominator of which is the Beginning Index.

If the Index is changed so that the base year differs from that used immediately preceding the month in which the term commences, the Index shall be converted in accordance with the conversion factor published by the United States Department of Labor, Bureau of Labor Statistics. If the Index is discontinued or revised during the term, such other government index or computation with which it is replaced shall be used in order to obtain substantially the same result as would be obtained if the Index had not been discontinued or revised.

5. Utilities and Taxes as Additional Rent. In addition to the ground rent specified in Sections 3 and 4 above, Sublessee agrees to pay the following costs and expenses as additional rent for the use and occupancy of the premises:

Tab B

RATE SUMMARY

Location	Contact	Phone #	Rental Rate per Month per Sq. Ft. Provided by Mr. Milligan	Rental Rate per Month per Sq. Ft. Provided by Listed Contact as of September 2008	Rental Rate Per Month Clarified by Mr. Lilly
Apple Valley Airport (KAPV)	Ans Scott/ Midfield Aviation	760-247-5766	12.5 cents	9 cents	9
Meadows Field (KBFL)	Wink Cecil	661-391-4906	15 cents	3.8 cents	8.1
Chino Airport	Tom Ricotta	619-987-6656	17 cents	N/A	19
Buchanan Field/Concord	Beth Lee	925-646-5722	10.8 cents	3.9 cents	10.8
El Cajon Airport	Cindy	619-562-3040	19 cents	8.5 cents	19
Hayward Air Terminal	Gary Briggs	925-200-0247	21.4 cents	2.75 cents	2.75
Fox Field/Lancaster (KWJF)	Steve Erving	661-940-1709	16.25 cents	13 to 14.4 cents	13 to 16.25
Van Nuys Airport	Bob Finkel	818-705-9861	30 cents	30 cents	30
Hawthorne Airport	Bruce McCall	310-676-4673	26 cents	20 cents	26
Mammoth Lakes	Pat Foster	760-924-9127	16.75 cents	15 cents	16.75
Riverside Municipal	Sharon	805-544-2450	20 cents	20 cents	20
Montgomery Field	Kevin O'Donnell	858-277-1453	14.4 cents	N/A	23.5
Palomar Airport	N/A	N/A	21 cents	N/A	21
Brown Field/San Diego	Tom Ricotta	619-987-6656	19 cents	N/A	19
San Luis Obispo Airport (KSBP)	Linda Butler	N/A	7 cents	N/A	7
Thermal Airport	Ann Goodwin	760-399-4300	12 cents	6 cents	12
Average Rental Rate			17.4	12.12 / 13.93	16.3

Tab C

Mullen & Henzell L.L.P.
ATTORNEYS AT LAW

RECEIVED FEB 21 2008

e-mail: glyons@mullenlaw.com



February 20, 2008

J. ROBERT ANDREWS
JEFFREY C. NELSON
JAY L. BECKERMAN
JOSEPH F. GREEN
MACK S. STATON
GREGORY F. FAULKNER
RICHARD G. BATTLES
EDWARD C. THOITS
WILLIAM E. DEGEN
MICHAEL E. CAGE
CHRISTINE P. ROBERTS
LORI A. LEWIS
PAUL K. WILCOX
MONICA M. ROBLES-MUZINICH
AMON R. GUPTA
RAFAEL GONZALEZ
JANA S. JOHNSTON
REBECCA D. EGGERMAN
LINDSAY G. SHINN

Frederick K. Glick, Esq.
1315 Santa Rosa Street
San Luis Obispo, CA 93401

Re: Sublease—Lilly/ Paso Robles Airport

Dear Mr. Glick:

I am in receipt of your February 7, 2008 letter regarding the ongoing negotiations between our respective clients at the Paso Robles Airport. I am also in receipt of Ms. Williamson's letter to Mr. Lilly dated February 7, 2008, informing Mr. Lilly that he is currently in default under his lease with the City. Given your client's outstanding issues with the City (and the direct impact these issues have on my clients), we do not believe mediation is an option at this time.

We await your client's resolution with the City.

Very truly yours,

A handwritten signature in black ink, appearing to read "Graham M. Lyons".

Graham M. Lyons of
Mullen & Henzell L.L.P.

THOMAS M. MULLEN
1915-1991

ARTHUR A. HENZELL
RETIRED

GML

G:\19468\0001\DOCS\CC4843.DOC

Tab D

ATTACHMENT No. 7 to Resolution No. _____



McDonough Holland & Allen PC
Attorneys at Law

Iris P. Yang
Attorney at Law

Sacramento Office
916.325.4576 tel
916.444.3826 fax
iyang@mhalaw.com

February 17, 2009

VIA ELECTRONIC AND FIRST-CLASS MAIL

William O'Connor
Morrison & Foerster LLP
12531 High Bluff Drive, Suite 100
San Diego, CA 92130-2040

RECEIVED

FEB 19 2009

MORRISON & FOERSTER LLP
SAN DIEGO

Re: Kim Lilly Subleases – Paso Robles Airport

Dear Bill:

Pursuant to our telephone conversation the other day, you requested that I let you know if the City had any comments on the form of the sublease that Mr. Lilly (through Fred Glick) submitted to the City for approval. The last version of the Sublease was the one that was faxed to Meg Williamson by Fred Glick on November 18, 2008.

As we discussed, the proposed form does not contain the proposed rental rate or term. We understand from our prior correspondence that Mr. Lilly is proposing rents of \$17.5 cents per square foot for a five-year term; 16.5 cents per square foot for a one-year term; and 14 cents per square foot for a month-to-month term.

In addition, the City does have some minor comments on the form sublease, as follows:

1. Section 5, third paragraph, second line, should read "CPI from the prior calendar year."
2. Section 5, fourth paragraph: The City uses the CPI Index for the San Francisco-Oakland area, rather than Los Angeles, for all of its leases.
3. Section 6, -- All signs should be approved by the City Planning Department, rather than the Airport Director.

Sacramento
555 Capitol Mall
9th Floor
Sacramento CA
95814-4692
tel 916.444.3900
toll free 800.403.3900
fax 916.444.8334

Oakland
1901 Harrison Street
9th Floor
Oakland CA
94612-3601
tel 510.273.8780
toll free 800.339.3030
fax 510.839.9104

1167633v2 32866/3004

www.mhalaw.com

Agenda Item 1 Page 86 of 87



February 17, 2009
Page 2

4. Section 12, please add the following paragraph:

"Sublessee, for himself, his heirs, personal representatives and assigns as a part of the consideration hereof, does hereby covenant and agree, as a 'covenant running with the land,' that in the event facilities are constructed, maintained or otherwise operated on the said property described in this lease for a purpose for which a DOT program or activity is extended or for another purpose involving the provision of similar services or benefits, Sublessee shall maintain and operate the Premises in compliance with all other requirements imposed pursuant to title 49, part 21, Non-Discrimination in Federally-assisted programs of the Department of Transportation Effectuation of Title VI of the Civil Rights Act of 1964, as said regulations may be amended."

5. Sections 19.1, 19.2 and 19.3 – these contain several references to the "Lease," which should be revised to refer to "Sublease."

6. Section 21: -- refers to a requirement to "carpet Premises." This does not seem appropriate for a hangar.

With the above textual changes, and subject to the City Council's acceptance of Mr. Lilly's proposed rents and terms, the proposed form sublease would be acceptable.

As I mentioned, the City Council is scheduled to have a special meeting on Wednesday, March 11, 2009, at 7:30 p.m. to consider the proposed subleases for Mr. Lilly's hangar sublessees. The approval process regarding these particular subleases has been unusual because in all prior instances, the parties have reached agreement upon the proposed terms, including rent and term, of the subleases before seeking approval. That was not the case here, and while the City does not have the authority to establish rents, it does have the legal obligation to ensure that the proposed rents are reasonable and non-discriminatory.

Please let me know if you wish to discuss this further.

Very truly yours,

Iris P. Yang
Iris P. Yang

IPY;jjh

cc: Meg Williamson
Roger Oxborrow
Fred Glick, Esq.