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Unico raises money for life after Metropolitan Tract

University of Washington's Metropolitan Tract faces new era

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Unico CEO Quentin Kuhrau stands in the Metropolitan Tract, the University of Washington-owned properties whose development was his company's reason for being. The Seattle firm is preparing for the 2014 expiration of its lease with the university.



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Photo Credit : Dan Schlatter



Photo Credit : Unico

Signing the Metropolitan Tract lease on July 18, 1953 is Roger L. Stevens, head of University Properties Inc. He is flanked by UW Regents Grant Armstrong, left, and Thomas Balmer. Standing behind them are, from left, John Spiller, secretary to the regents; H. Adams Ashforth, a New York investor; and Regent Arthur T. Lee.

As Unico Properties nears the end of the 60-year lease that put the firm in charge of a large swath of downtown Seattle, the company is reinventing itself for its independent new life.

Unico's deal to manage the Metropolitan Tract for owner University of Washington expires in four years. The Seattle firm is now gearing up to expand its own real estate portfolio through a \$750 million real estate investment fund.

The company plans to use the new fund to add to the hefty collection of non-UW holdings it has assembled in recent years — 33 office and residential buildings totaling more than 8.3 million square feet in nine metropolitan areas. A couple of years ago, Unico even turned a pair of factory-built modules into a prototype for ultra-affordable apartments that the company dubbed “inhabit” before putting the avant garde project on hold pending better credit conditions.

Unico's expansion thrust traces to the early 1990s, when its owners started thinking about what the firm should do when its original reason for being — the UW Metropolitan Tract ground lease — expires in 2014.

“They made the decision to build the company,” said current CEO Quentin Kuhrau. “‘Life after 2014’ became the rallying mantra within the company.”

Kuhrau was part of a management team, also including Dale Sperling, John Bliss and David Laird, brought in in 1996 to build that broader platform.

The UW partnership, dating back to 1954, led to Unico managing five buildings totaling 1.5 million square feet on land that had mostly been donated for the original university campus in what is now the heart of downtown Seattle.

After the university moved from the tract in 1895 to its spacious present campus five miles north, UW regents voted to lease the tract properties rather than sell them. In 1907, UW leased the tract to the Metropolitan Building Co., which hired a New York firm to create a master plan for developing the tract.

[Unico Properties LLC](#) initially was known as University Properties Inc. and was formed in 1953 after the UW tapped Roger L. Stevens — onetime owner of the Empire State Building — and a group of private investors to develop the school's downtown holdings under a subsequent long-term ground lease.

Unico took over management of the university's Cobb medical office building, its luxurious Olympic Hotel and the Skinner Building, home to the ornate Fifth Avenue Theatre. Unico then set to work developing more modern office spaces on the tract — Puget Sound Plaza (built in 1959), the IBM Building (1964), Financial Center (1970) and Rainier Tower and Square (1977).

The UW contract allowed Unico to be entrepreneurial in developing the tract but required continuous reinvestment in tract properties over the period of the lease. It was “a pretty unique revenue-sharing arrangement,” Kuhrau said, that shifted the risks inherent in developing the tract from the state university onto a private party.

“It was not appropriate for a public body to take on a lot of risk,” Kuhrau said.

In fact, Kuhrau said, Unico did not start making significant money on the deal until the 1990s, when its debt for developing the buildings was finally retired. Kuhrau would not disclose specific profit numbers.

“Forty of those 60 years were really about plowing revenue receipts back into the tract to build new buildings and to pay off debt,” Kuhrau said.

In more recent years, he said, Unico has been able to reap an undisclosed amount of profit from its portion of the tract's cash flow.

Unico's long-term ground lease expires in 2014, giving UW the choice of again hiring out the management and development of the tract, or operating the tract on its own.

Unico will bid to manage the tract, Kuhrau said, if the UW decides it wants to continue outsourcing that job. The school recently named a blue-ribbon Advisory Committee on Real Estate to guide it on how to best take advantage of its property treasures.

According to a recent legislative report, the Metropolitan Tract generated \$10.7 million for the university last year in cash flow from operations. The school's average annual income return on investment from the tract over the past decade has been 4.8 percent. However, also taking property value appreciation into account, the 10-year average return reaches 14.2 percent, according to the legislative report.

Kuhrau agrees with those who say that UW could make more money from the tract under a new arrangement.

The current lease is structured to encourage development of the tract, “which is not really as meaningful today as it was in the 1950s,” Kuhrau said. Estimates that the tract could yield an additional \$5 million to \$10 million a year for the UW are “about right,” he said.

The Unico CEO expects the university likely will draft a more traditional property management contract that maximizes cash flow to the campus.

Any new developments on the tract would likely come under separate contracts that would shift development costs and risks to a third party in return for a ground lease on that specific property.

Kuhrau said Unico will be leaving the Metropolitan Tract in good order when the contract ends. Vacancies are under 10 percent, which is better than the overall market, which has vacancies of nearly 18 percent.

Unico is required to pour at least 3 percent of the tract's gross revenue back into maintenance and repair, but the company typically has exceeded that amount, Kuhrau said.

For the past three years, Unico has put more than 7 percent of gross revenues into keeping up the properties, including an \$8.5 million overhaul of the mechanical systems in Puget Sound Plaza and the Skinner and IBM buildings. The renovation yielded \$1.6 million in energy rebates from the city and earned all three properties LEED gold ratings, the second-highest available under the U.S. Green Building Council's Leadership in Energy and Environmental Design program.

Competition to replace Unico in managing the tract likely will be fierce.

"There would be a lot of players interested in that — we're talking about one of the most high-profile parcels in a downtown area, probably in North America," said Kip Spencer, co-founder of OfficeSpace.com and director of business development in the Kirkland office of JE Dunn Construction.

Office rents in the tract are in line with other asking rents in the central business district, ranging from \$24 to \$36 a square foot. Tenants include Kennedy Associates, Hacker Group, IBM, the King County Bar Association and the Seattle Foundation, according to Unico's website.

Dan Flinn, a principal at Seattle-based Flinn Ferguson Corporate Real Estate, said the tract properties are well-maintained, well-located and competitive with other Class A downtown office properties, including newly built towers. The tract office buildings have an additional advantage.

"Their vacancies are not so significant," Flinn said, "so they have the ability to mitigate their vacancies by re-leasing space in smaller chunks. They don't need to sign a 200,000-square-foot deal — they just need to lease 5,000- to 10,000-square-foot spaces, and there are more tenants in that size range, generally."

Kuhrau also believes the location of the tract near downtown cultural attractions and shops makes the properties competitive with newer office towers.

Unico has no plans to redo either of the two best remaining sites for potential redevelopment — Puget Sound Plaza and the north end of Rainier Square. There is neither the market nor sufficient time before the lease expires, Kuhrau said.

As it prepares for life untethered to its UW partner, 100-employee Unico plans to raise its new investment fund with financial backing from the wealthy private investors and institutional

investors that Unico has worked with over the past 15 years in buying properties, said Kuhrau, who was promoted to CEO earlier this year.

Prior institutional partners include JP Morgan, LaSalle Investments, Cigna Life Insurance and Citibank among others.

Kuhrau said the company will use the fund to purchase or develop properties in the Western United States over the next two or three years to take advantage of the current drop in real estate property values.

The company's strategy would be to buy and hold the properties, Kuhrau said.

"This will lift us to the next level of growth," Kuhrau said. "We see great opportunity to invest in the current cycle."

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