

VII. STANDING COMMITTEES**B. Finance, Audit and Facilities Committee**

in Joint Session with

A. Academic and Student Affairs Committee**Revision of UW Medicine South Lake Union Phase III Option Agreement****RECOMMENDED ACTION:**

The administration and the Finance, Audit and Facilities Committee recommend that the Board of Regents authorize the President or his designee to execute the Revised Option Agreement for South Lake Union Phase III that has been negotiated by representatives of City Investors LLC, City Investors XII LLC (“City Investors”), and the University of Washington.

BACKGROUND:

On April 17, 2003 the Board of Regents approved proceeding with development of new biomedical research space in South Lake Union under a long-term lease structure, beginning with the renovation of the former Washington Natural Gas headquarters (the “Blue Flame” building, subsequently renamed the Brotman Building) as Phase I. The Board also approved a Phase II Option Agreement which would enable the University to expand into additional buildings to be constructed on the remainder of the Blue Flame block, and a Phase III Option Agreement providing for additional expansion of up to three buildings on an adjoining block if warranted by growth in space demand and research funding.

The Brotman Building is approximately 110,000 gross square feet in size. The building’s renovation was completed in December 2004, and it is now occupied by School of Medicine research programs in biomedicine and related fields. On March 17, 2005, the Board of Regents approved proceeding with the Phase II development, consisting of approximately 300,000 gross square feet of new construction to provide space for office and laboratory uses and a below-grade parking facility serving both the Phase II buildings and the Brotman Building. The Phase II buildings are now under construction, and the project is on budget and on schedule for completion in the summer of 2008.

Under the terms of the Phase III Option Agreement, the University has the ability to exercise the option in up to three sub-phases. Exercise of the option for the first sub-phase is due in September 2007, while exercise of the option for the third sub-phase is due by June 2009. Based on this schedule, completion of the Phase III buildings would take place between 2011 and 2013. During the development of Phases I and II, it became clear that this option schedule and development timeframe would be unworkable for the University. Accordingly, University representatives initiated discussions with the landowner (City Investors) regarding possible revisions to the Option Agreement to extend the option period and provide for a significantly longer

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time period for development of the Phase III buildings. City Investors was willing to accommodate the University's requests, so long as the changes were revenue-neutral to them and provisions were incorporated to assure that the Phase III site would be developed in a coordinated and timely manner.

As renegotiated, the Revised Option Agreement contains the following key terms:

- The option expiration date is extended to March 15, 2010;
- In the interim, the University will pay the same amount in option fees as would have been paid as a combination of option fees and ground rent under the original Option Agreement (amounts that increase each year, from approximately \$1.3M in FY2008 to approximately \$1.6M in FY2011);
- During the option period the University will incur up to \$500,000 in initial planning expenses that would have been incurred under the original Option Agreement;
- Exercising the Option commits the University to the full development of Phase III, approximately 365,000 square feet, with anticipated building completions in December of 2012, 2015, and 2018 respectively; and
- If the University elects not to exercise the Option, an additional deferred option fee of between \$1M and \$4M would be paid, depending on when notice of the decision not to proceed is given. The revised Option expiration date will allow the University to make a final decision as to whether to proceed with Phase III in early summer of 2009, after the legislative session has concluded, in which case the deferred option fee would be \$2,000,000 if the University decides not exercise the Option. If the University waits until the end of the Option period (March 15, 2010) to notify City Investors that it is not exercising the Option, the deferred option fee would be \$4M.

The revised Option Agreement preserves the University's ability to address the School of Medicine's compelling strategic need for additional research facilities in the future, at a reasonable cost given the size and location of the Phase III site. It provides additional time for the University to assess research funding trends, continue private fundraising efforts, and work for ongoing state funding in support of research facilities.

The Revised Option Agreement for Phase III has been recommended for approval by the Executive Vice President for Medical Affairs, the Executive Vice President, and the Director of Real Estate.