

PORT OF SEATTLE
MEMORANDUM

COMMISSION AGENDA
ACTION ITEM

Item No.	<u>6d</u>
Date of Meeting	<u>June 25, 2013</u>

DATE: June 12, 2013

TO: Tay Yoshitani, Chief Executive Officer

FROM: James Schone, Director, Aviation Business Development
James Jennings, Manager, Aviation Properties
Wayne Grotheer, Director, Aviation Project Management Group

SUBJECT: United Services Organization Northwest Lease and Associated Second Floor Utilities Preparations (CIP #C800615) Authorization

Amount of This Request: \$2,666,000 **Source of Funds:** Airport Development Fund

Est. State and Local Taxes: \$169,000 **Est. Jobs Created:** 41

Est. Total Project Cost: \$2,666,000

ACTION REQUESTED:

Request Commission authorization for the Chief Executive Officer to (1) execute a lease, substantially as drafted in the attached Exhibit 1, with the United Services Organization Northwest (USO) for a term of ten years, with two five-year options, for operation of the Airport service members' lounge located in the Main Terminal of the Seattle-Tacoma International Airport; (2) complete design of the Second Floor Utilities Preparations project at Seattle-Tacoma International Airport; (3) advertise and execute major construction contracts; and (4) utilize Port crews. The total amount of this request is \$2,666,000, which is also the total projected program cost.

SYNOPSIS:

The USO Center has been open at the Airport since 1968 and has the highest volume of USO visitors of any airport in the country. It provides 24/7 travel assistance and "all the comforts of home" to traveling servicemen and women and their families. There is not enough space in the USO's current location to meet the current and future needs of USO patrons.

Commission authorization is requested for staff to execute a long-term lease with the USO for a new location on the second floor of the original 1947 Terminal Building at the Airport. The 10-year lease will include two additional five-year options for the tenant to extend, for a total potential period of 20 years. This lease requires the USO to make an investment of \$1.2 million of their own capital funds for their tenant improvements, which is not included in the Port's costs

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for this project. This lease also commits the Port to spend approximately \$1.271 million of the requested \$2.666 million capital project in the design and construction of a building envelope and associated utilities and infrastructure for the new USO to be brought to its lease line. The remaining \$1.395 million project cost is largely to provide future utilities for the remaining vacant second floor space. Relocating the USO from the south mezzanine level to this central location will provide valuable office space for current and future airlines that is more proximate to ticket counters and locates the USO in a larger space to accommodate its needs. At the advice of counsel, this request seeks a single Commission authorization for design, advertisement and execution of a major construction contract to demonstrate the Port's financial commitment in executing the lease.

This project was included in the 2013 – 2017 capital budget and plan of finance as an element of the Mezzanine Tenant Relocation project, CIP C800560, a business plan prospective project with a budget of \$5 million.

BACKGROUND:

The USO center has been open at the Airport since 1968 and currently serves 10,000 service members, families, reservists and retired military a month. Continuing 45 years of service, the USO center provides 24/7 travel assistance and access to all the comforts of home: hot meals, snacks, a TV lounge to rest and relax, a shower, and free Internet access to service members of all branches of the military and their families. With proximity to several military installations (Joint Base Lewis-McChord, Puget Sound Naval Shipyards, Bangor Submarine Base, Everett Naval Station and Whidbey Island Naval Air Station), the Airport is a vital corridor for service members traveling to other duty stations around the world. There are unique characteristics of the military community that travels through the Airport:

- Air Mobility Command (AMC) is the military's official air transport unit that coordinates flights for duty station movements and relocations of active service members and their families. AMC has regular flights every week to support these movements.
- Active service members are often on specific orders that require reporting to the Airport up to 24 hours in advance of their proposed flights.
- Duty station movements often include significant luggage, including large duffel bags, household pets, and often family members' belongings.
- With the significant luggage and extended layover times, the amount of space required for luggage storage is significant.

These passengers spend much of their time waiting to be ticketed and, without the USO at the Airport, would be forced to utilize the very limited amount of passenger circulation space pre-security on the ticketing level. With the large number of military personnel and their families at the Airport on a daily basis, for long lengths of time and with significant amounts of luggage, their presence in the ticketing area would substantially increase terminal congestion.

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The current USO is 3,410 square feet and is located toward the south end of the mezzanine level of the Airport, which is one level above the ticketing level (see Exhibit 2). The Port currently has a month-to-month agreement with the USO for the lease of this space.

In early 2012, the USO requested a long-term lease from the Port to assist in their capital fund raising efforts and to enable the amortization of a potentially significant tenant improvement project. Their initial capital investment was intended to update and improve their current space on the mezzanine level above ticketing, formerly used as the World Trade Center lounge. But concurrent with their request, Port staff was working on developing the scope of the Mezzanine Tenant Relocation project (approved by Commission on March 26, 2013). This plan was developed to meet the increased demand for airline office space at the south end of the main terminal building. So, in coordination with this planning effort, the Port proposed to move the USO from their current mezzanine location to the second floor of the original 1947 Terminal Building as part of this plan (see Exhibit 2). This move creates an additional 3,410 square feet of office space available on the south end of the mezzanine level, which has already elicited significant interest from one of our larger airline partners. Additionally, the increase in space allocated to the new USO to 7,000 square feet will provide needed area for additional seating, sleeping, showers, laundry, and luggage storage.

In conjunction with the request to execute a lease with the USO, this request also seeks authorization for design and construction funding for the previously recommended improvements in the amount of \$2.666 million (CIP #C800615). This project will create a shell and utilities for the USO to construct their tenant improvements in the new space so that they can vacate their current location, freeing up valuable space at the south end of the mezzanine level that can be used by airlines for office space. The new USO location is in an area that doesn't have as much proximity to airline operations. This project also includes adequate electrical, mechanical and HVAC capacity for the remainder of the vacant second floor space (see Exhibit 3).

An essential element of an airline's operation at the Airport is office space located pre-security to support the airline's ticketing functions. The proximity of this office space to the ticket counters is highly important for operational efficiency. The Airport has limited pre-security office space to support current and future airline needs. Aviation Business Development recently completed a study of office space in the main terminal building. This study highlighted the scarcity of suitable space. This project will create suitable office space for the USO, which will in turn free up space that is in proximity to the ticket counters.

The capital portion of this lease was originally part of the Mezzanine Tenant Relocation Project (CIP #C800560), with a total capital project budget of \$5 million. Because of timing differences and the complexity of the USO lease and tenant improvements, the project was split into two separate projects in early 2013. The budgets of these two projects (Mezzanine Tenant Relocation Project and the USO Second Floor Utilities Preparation projects) if recombined would be less than the original \$5 million budgeted in the 2013-2017 capital budget and plan of finance.

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LEASE SUMMARY:

Below is a comparison of the key business terms of the current lease and new, proposed lease. The full version of the new, proposed lease is attached as Exhibit 1:

	Current Lease	Proposed 10-year lease
Term	Month to Month	Ten years
Extension	Not Applicable	Yes, Two, five-year options for the tenant to extend
Holdover	Not Applicable	Yes, Month-to-month
Square Footage	3,410 square feet	~7,000 square feet
Rent	None	\$10.00 per year
Tenant Improvement	None	\$1.2M
Electric Utilities	No charge	Pay \$36.50/mo. (base electrical rate) plus anything above agreed upon max threshold to incentivize conservation
Other Utilities	No charge	No charge

PROJECT JUSTIFICATION:

With limited pre-security office space in the terminal to support current and future airline needs, the current USO office space is better utilized as office space by current and possibly future airlines at the Airport. In accordance with the Century Agenda goal to double the number of international flights and as the Airport anticipates continuing strong international growth, Port staff is working to relocate non-airline tenants to better accommodate pent up demand from current airlines as well as accommodate the likely addition of new international carriers in the not too distant future.

Additionally, with over 120,000 visitors to the Sea-Tac USO annually – the highest volume airport USO in the United States – there is not enough space to accommodate the current and future needs of the USO patrons. There is insufficient luggage storage space for frequent peak times and excess luggage is currently stored outside the USO in temporarily unused office space. Most notably, during peak times, service members and their families spill out onto the mezzanine circulation corridor, causing congestion.

There is approximately 17,500 square feet of currently unleaseable space on the old second floor of the 1947 Terminal Building that can accommodate the relocation of the USO. This new USO would use approximately 7,000 square feet of this available space. This space is currently

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unleasable, primarily due to lack of basic utility infrastructure capacity including ventilation air and electrical power. This project will not only provide these utilities to the USO but also to the remaining unleaseable space, thereby rendering it usable for the future. Abatement in this area will not be completed and there will be no architectural shell finishes as part of this project scope in preparation for a future use or lease. This area is not considered desirable for the airlines because of its location and access challenges, as well as the need for a significant capital investment by the tenant. Therefore, with the USO's desire for a long-term lease, the unavailability of additional space adjacent to their current mezzanine location, and willingness to take on a significant tenant improvement project, the proposed lease and capital project request resulted.

Project Objectives:

- Partner with the USO to provide a long term place for the USO in the main terminal.
- Free up valuable mezzanine level space that can be used for airline offices that need to be proximal to ticketing by moving the USO from their existing location.
- Provide adequate electrical, mechanical and HVAC utilities for the future build-out of the remainder of the unoccupied and underserved second floor space.

PROJECT SCOPE OF WORK AND SCHEDULE:

Scope of Work:

- This project will provide adequate utilities (electrical, data/communications, mechanical and HVAC capacity) for this entire uninhabitable vacant space of the second floor.
- Utilities will be brought to the second floor space.
- This project will construct shell walls for the USO so that they can construct a tenant improvement (TI) of approximately 7,000 square feet and relocate from their existing mezzanine level space.
- This project will address building code egress issues for expected future office occupancies for the second floor through design considerations of the egress pathways.
- Utility connections to serve the new USO TI will be located and agreed to by both the Port and the USO.
- This project will abate regulated materials impacted by the USO Tenant Improvement construction only.

Schedule:

Commission Authorization	July	2013
Begin Design	July	2013
Port abatement and building of shell demising wall	July	2013
USO Begin TI Construction	November	2013
Advertise Construction Contract	December	2013
Begin Construction	March	2014
Project Completion	July	2014

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FINANCIAL IMPLICATIONS:

Of the \$2.666 million in costs forecasted for this project, 48%, or roughly \$1.271 million has been allocated to the USO relocation for the purposes of this financial analysis. Weighing that cost against the revenue stream associated with a paying tenant in the space vacated by the USO, the project's net present value over a 10- year period is slightly positive.

<i>Budget/Authorization Summary:</i>	Capital	Expense	Total Project
Original Budget	\$2,545,000	\$121,000	\$2,666,000
Previous Authorizations	\$0	\$0	\$0
Current request for authorization	\$2,545,000	\$121,000	\$2,666,000
Total Authorizations, including this request	\$2,545,000	\$121,000	\$2,666,000
Remaining budget to be authorized	\$0	\$0	\$0
Total Estimated Project Cost	\$2,545,000	\$121,000	\$2,666,000

<i>Project Cost Breakdown:</i>	This Request	Total Project
Construction	\$1,781,000	\$1,781,000
Construction Management	\$268,000	\$268,000
Design	\$178,000	\$178,000
Project Management	\$234,000	\$234,000
Permitting	\$36,000	\$36,000
State & Local Taxes (estimated)	\$169,000	\$169,000
Total	\$2,666,000	\$2,666,000

Financial Analysis and Summary:

CIP Category	Revenue/Capacity Growth
Project Type	Business Expansion
Risk adjusted discount rate	7%
Key risk factors	Low risk associated with releasing existing USO space
Project cost for analysis	\$2,660,000
Business Unit (BU)	Aviation Business Development
Effect on business performance	NOI after depreciation is expected to be positive
IRR/NPV	For the \$1,271,000 attributed to the USO, we have calculated a positive NPV of \$484,000 based on the projected revenue stream of the space vacated on the Mezzanine. For the remaining space there is no known revenue stream.
CPE Impact	Increase of less than \$.01

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Budget Status and Source of Funds:

As indicated above, this project was included in the 2013-2017 capital budget and plan of finance as a business plan prospective project within the Mezzanine Tenant Relocation project CIP #C800560. The funding source will be the Airport Development Fund.

Lifecycle Cost and Savings:

The lifecycle cost and savings of this project will be determined and finalized as an element of design. It is anticipated that opportunities for savings exist with the planned utilities installation and systems to be installed as part of the tenant work. Annual Operating and Maintenance Costs will increase due to increased use of space and utilities.

STRATEGIC OBJECTIVES:

This project promotes the Port's Century Agenda objective of meeting the region's air transportation needs at Sea-Tac Airport for the next 25 years by adding capacity for office space within the existing main terminal building. As the Port strives to develop new business and serve 45 million passengers annually, including doubling the number of international flights, it is important to provide office space near airline ticketing operations so the airlines can conduct business efficiently.

ENVIRONMENTAL SUSTAINABILITY:

This project will examine in detail the following aspects during design: water use reductions, including low flow fixtures, energy performance heating ventilating and air conditioning equipment, potential for materials reuse and recycling, and factors to improve the indoor environmental quality. Additionally, the lease will establish a financial structure to promote electrical conservation.

BUSINESS PLAN OBJECTIVES:

This project supports the Aviation Division's strategic goal of operating a world class international airport by anticipating and meeting the needs of our tenants, passengers, and the region's economy. It facilitates better use of mezzanine office space by locating airline offices closer to their operations and relocating current non-airline tenants to spaces more suitable for their needs. It also supports one of our important community partners, the USO, in enhancing its mission to provide an important service to these critical members of our community and their families.

TRIPLE BOTTOM LINE:

The approval of this lease and the associated project supports economic development through freeing up valuable airline leasable space at the Airport. Environmental sustainability principles will be employed in the design and construction of both the Port and USO's tenant improvement projects, as well as create financial incentives in the USO lease to incentivize conservation of utilities. Also, the mission of the USO has a significant community benefit through providing important support to these important service members and their families.

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ALTERNATIVES CONSIDERED AND THEIR IMPLICATIONS:

Alternative 1 – Do nothing - the current USO lease will continue indefinitely. The USO would have to consider investment in the existing location without the necessary additional space to meet their future needs. Existing airlines may not have office space available or in a location that is necessary for an efficient airline operation. This is not the recommended alternative.

Alternative 2 – Authorize execution of a new lease with USO but require the USO to complete necessary utility improvements and forego utility improvements in the remaining facility space. This alternative would put an excessive financial burden on the lessee, and require the USO to construct improvements outside of its leased area, which is not consistent with Port policy. This is not the recommended alternative.

Alternative 3 – Authorize execution of a new lease with the USO but not invest in the utility improvements for remaining facility space. With the likely demand for this remaining space likely to be needed in the near to mid-term future, making these utility improvements as part of a future project, this alternative would increase construction costs as well as provide an additional time barrier to the future use or lease. This is not the recommended alternative.

Alternative 4 – Authorize execution of a new lease with USO and invest in utility improvements to the remaining facility space. This alternative will lead to a better customer experience, increase our readiness for future space needs, and enhanced revenues due to a relocated and upgraded service members' lounge facility. **This is the recommended alternative.**

OTHER DOCUMENTS ASSOCIATED WITH THIS REQUEST:

- Exhibit 1 – Proposed Draft Lease Agreement.
- Exhibit 2 – USO Existing vs. Proposed Site
- Exhibit 3 – Proposed USO Site vs. Remaining Vacant Space

PREVIOUS COMMISSION ACTIONS OR BRIEFINGS:

- None