

# CityNorth projects all had troubled launches

by **Max Jarman** - Jan. 10, 2010 12:00 AM  
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At the \$300 million CityNorth development in northeast Phoenix, parking spaces are plentiful along the Main Street equivalent known as High Street.

On a recent weekday, a handful of shoppers strolled sidewalks of the four-block-long thoroughfare, meandering in and out of the 14 stores that remain open.

CityNorth was supposed to be Phoenix's hottest new destination, with luxury condominiums, chic boutiques and, in its second phase, the area's first Bloomingdale's department store.

It now sits in foreclosure, unable to pay back loans to its bankrupt lender, the victim of frozen credit markets, plunging retail sales and collapsed real-estate values.

CityNorth joins a handful of visionary but ill-timed commercial real-estate projects that were spectacular initial failures. They include the Camelback Esplanade mixed-use development and the once-luxurious Scottsdale Galleria shopping mall.

Over the long term, those projects evolved differently yet successfully.

Ultimately, developer and former Gov. Fife Symington's vision for the 22.5-acre site at 24th Street and Camelback Road was fulfilled by investors who bought the Esplanade project for pennies on the dollar at a public sale in 1994. Its buildings now command some of the top rents in metro Phoenix.

But the Galleria, Amram Knishinsky's 1987 dream of a 1.35 million-square-foot shopping mall with 245 trendy stores at Fifth Avenue and Scottsdale Road, was not realized.

Thomas J. Klutznick envisioned CityNorth as a vibrant urban center in the middle of the 5,700-acre Desert Ridge community for which his company is the master developer.

And most real-estate experts agree that the CityNorth site at 56th Street and the Loop 101 remains one of the area's choice commercial locations. As with the Esplanade and Galleria, new investors, along with evolving market conditions, will help shape its still-uncertain future.

## **Echoes of Esplanade**

Like Klutznick's vision for CityNorth, Symington's dream of an upscale office, retail and residential development at 24th Street and Camelback Road was controversial and fraught with high-pitched zoning battles.

Symington spent \$200 million to develop two 11-story office buildings and the 281-room Ritz-Carlton hotel that opened in 1988. After the savings-and-loan crisis and resulting real-estate crash, the hotel and office buildings were sold in 1994 for \$69 million to a Boston investment adviser.

An undeveloped 12 acres, zoned for retail shops, three more office towers and a high-rise condominium building were purchased for \$6 million by Francis Najafi's Pivotal Group and Southwest Value Partners, headed by Phoenix Suns owner Robert Sarver. They partnered with Opus Southwest to built three office buildings, a condominium tower, retail and restaurant space and a movie-theater complex.

Attorney Grady Gammage said it's common for such major projects to go through several developer/owners, and even foreclosure, because they are long-term projects that often span several real-estate cycles.

Gammage said Camelback Esplanade ultimately succeeded because of the quality of the site and the development plan.

### **Galleria concept flops**

The Scottsdale Galleria was ill-conceived from the beginning, Gammage said.

The anchorless center was supposed to attract high-end boutiques, many by European designers, which would draw customers. The center with marble floors, brass fittings and a huge open atrium opened in 1991 and closed in 1993. The Galleria languished for years as owners struggled with what to do with the property.

Excel Realty trust, which bought the \$130 million center for \$6 million at a 1993 foreclosure, kicked out the tenants, sold off the computerized fountain that pulsed with music, ripped out the marble and scraped the brass fittings. The failed mall went through a number of subsequent owners, whose unsuccessful proposals for the property included a sports-related mall, Wild West theme park and branch of the Smithsonian. It's now a successful office building with tenants that include health-care-services provider McKesson Corp.

### **Bad timing**

CityNorth is being developed by a partnership between the Klutznick Co. of Chicago, New York's Related Cos. and JER Partners of McLean, Va.

High Street opened in November 2008, weeks after the national economy began to seriously unravel.

The market for the luxury condominiums dried up. Retailers waited for customers that never came. Stores without staying power skipped out or never moved in. Others, primarily national chains, are sticking it out, at least until their leases expire.

But some things are working. All of the unsold condominiums have been rented as apartments, and the Related Cos., which manages the project, reports decent demand for office space.

The dozen or so restaurants and bars are not doing as well as they expected, but "much better" than the retail stores, according to Andrew Whitman, manager of the Kona Grill restaurant at CityNorth.

The CityNorth foreclosure includes only the 24-acre High Street phase of the development, which comprises 180,000 square feet of retail and restaurant space, 330,000 square feet of offices and 99 condominiums.

Capmark Financing Inc. is now foreclosing on a \$290 million loan that is secured by the 627,000-square-foot retail, office and residential project.

Klutznick Co. principal John Klutznick, Thomas' son, said he has been working with Capmark to secure a buyer to take over the project and inject fresh capital.

Klutznick declined to name any of the project's prospective buyers but said there has been considerable interest.

A second phase of the project which includes 773,000 square feet of retail and restaurant space plus more condominiums and offices is unaffected by the foreclosure and will continued to be developed by the Klutznick Co. The second phase was slated to open this year with Bloomingdales, Nordstrom and Macy's department stores but has now been postponed until the economy improves.

A controversial deal with Phoenix that allows Klutznick to recover \$97 million in sales taxes generated by the development is tied to that phase of the project. A lawsuit filed by the Goldwater Institute resulted in the deal being declared unconstitutional. The Arizona Supreme Court heard an appeal but has yet to issue a ruling.

## **Buyer interest**

A March 31 foreclosure sale likely will result in new owners who could nurse the project through the current economy adhering to Klutznick's vision. Or the project could shift its focus, with more offices and restaurants and fewer retail shops.

Market analysts are optimistic that the fundamental strength of the CityNorth concept and location will ensure its ultimate success.

"The market is tough right now, but CityNorth is such a great piece of property that it will be worked out," said Marty DeRito, president of DeRito Properties, a retail property brokerage and development firm.

## **More on this topic**

### **CityNorth, Phase I**

- Upscale retail, office and condo development, 56th Street and Loop 101.
- Developer: Klutznick Co., Related Cos. and JER Partners.
- Cost: \$300 million.

- What happened: Foreclosure proceedings started on \$290 million loan secured by the development. Property set for a trustee's sale March 31.

### **Scottsdale Galleria**

- Upscale shopping mall, Fifth Avenue and Scottsdale Road.
- Developer: Melvin Simon & Associates and Scottsdale Galleria. Ltd.
- Cost: \$130 million.
- What happened: Opened in 1991, sold for \$6 million at a foreclosure sale in 1993 and closed. Now an office building.

### **Camelback Esplanade**

- Mixed office, residential, retail development, 24th Street and Camelback Road.
- Original developer: The Symington Co.
- Cost: \$200 million, first phase.
- What happened: Two office buildings and Ritz-Carlton hotel sold for \$69 million in 1994. An undeveloped 12 acres went for \$6 million. Now a metro Phoenix landmark.