

Ireland's Cork School of Music PPP

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Cork's €72.7m (US\$86m) music school PPP serves as the ultimate example of a survivor. After over five years in the making, the ex-Jarvis project was successfully closed on 5 September 2005 by Hochtief and Barclays as Ireland's third ever education PPP

The project was given the go-ahead by the Irish government as back as 2000 but, since then, planning delays, funding shortfalls, EU regulation and the difficulties faced by its original preferred bidder Jarvis have put it through the ultimate endurance test.

Hochtief PPP Solutions eventually saved the deal by acquiring Jarvis' PPP bidding arm in November 2004, and so Jarvis' interest in the project - becoming de facto preferred bidder for the 25 year DBFO contract.

The deal - sponsored on a 50:50 basis by Hochtief PPP Solutions (Ireland) and Barclays Private Equity (BPE) - is also the first accommodation PPP to have closed in Ireland for 18 months.

Peter O'Shea, project director for Hochtief - and formerly Jarvis - says: 'The project also stands out because it's a third level school and there is no other music and movement college of that nature in Ireland.'

Background

Plans for a PPP revamp of 130 year-old Cork Music School building were first announced by the Irish Minister for Education & Science in October 1999.

In June 2000 the department launched the DBFO tender and shortlisted three bidders: Jarvis, Bovis Lend Lease and a local consortium headed-up by Clayton & Love.

All proposed the demolition of the existing building and its replacement with a new structure as the most cost effective way forward. Jarvis - proposing a new custom designed facility - was eventually selected as the preferred bidder for the project in 2001.

However, it was at this stage that the project ran into difficulties. Firstly, a planning objection by an Irish heritage group delayed the project. Then a dispute over the treatment of PPPs in Government accounts and a subsequent wrangle with the EU threatened to derail the project.

On this second major hurdle, Hochtief's Peter O'Shea explains: 'The Irish department of finance questioned if accommodation PPPs could legitimately be considered off-balance sheet deals, as they didn't carry demand risk and asked the EU for clarification.

Then, eventually, the Eurostat finding stated that all accommodation PPPs, to qualify as off-balance sheet deals, had to

take construction and availability risks, but not necessarily demand risk.' he adds. 'With two of these three risks covered, accounting to over 50 per cent of total risk, they qualify.'

After a delay of over 18 months due to this process, the Cork deal could move on - with construction and availability risks assumed but not demand risk, as usual in non-road deals.

Following the EU review of the accounting treatment of PPPs, amendments were introduced that recognised the long term nature of such projects and in July 2004 the government decided to give the go-ahead to enter into detailed final negotiations with Jarvis.

Unfortunately, by this time Jarvis started to experience financial difficulties and - teetering on the verge of collapse - was not able to secure financing.

In late 2004 Hochtief Developments, looking for a foothold in UK and Irish PPP markets, stepped in to purchased the PPP Bidding Arm of Jarvis and in effect took over the project.

The changeover added a new impetus to the project and opened the way for detailed negotiations between Hochtief, the Department of Education and Science and Cork Institute of Technology (CIT), leading ultimately to the signing of the contract.

Discussions were based on Jarvis' original bid. Peter O'Shea comments: 'It was a fairly seamless transition. The project was just revised and fine-tuned, working closely with the CIT.'

Hochtief not only worked with the bid's original bank - Barclay's - but also maintained the same design team and most advisers.

The project

The project involves the construction and facilities management for 25 years from completion of a new, specialist music school for the Irish Department of Education and Science. The new school is to be built on the grounds of the existing school, on Union Quay in the centre of Cork City overlooking the river Lee.

The 5-storey music school building will have an area of around 10,500 square metres and will accommodate up to 400 full-time and 2,000 part-time students.

Facilities will include specialist tuition rooms, lecture rooms, a rehearsal hall, an auditorium capable of seating 500 people, a recording studio, drama suite and library with reading rooms.

The project company - CSM PPP Services - will also equip and operate the complex, with Hochtief FM operating the facilities post construction.

The facilities management contract comprises both hard services such as upkeep, maintenance and energy management, and soft services such as cleaning of the building and gardening.

Construction works started on 12 September 2005 and are carried out by local subcontractor John Sisk & Sons, the largest contractor in Ireland. Building work is scheduled to be completed by September 2007.

The exact capital value all-in amounts to €68m (US\$81.4m), including a €46m (US\$55m) construction contract with Sisk.

Financing

Financial close was reached on September 2005 with Barclays Bank as sole arranger and Hochtief PPP Solutions (Ireland) and Barclays Private Equity (BPE) each holding 50 per cent of the equity.

The total project cost amounted to €72.7m (US\$86m as of 30/12/2005). Total debt was €65.1m (US\$77) and equity amounted to €7.6m (US\$9m).

The financial adviser to the project company was David Wylde Project Finance, while Farrell Grant Sparks was financial adviser to the government.

A source at Barclays involved in the deal said: 'Barclays worked on the transaction right from when Jarvis originally won the deal in 2001. It was an interesting deal in that it involved specialist music rooms and specialist equipment, however, it was financed using a classic PPP structure.'

'The bank had to get comfortable with procurement issues regarding the replacement of Jarvis, and replacement of FM provider.'

Hochtief's Peter O'Shea comments: 'Legal and financial due diligence were quite fast considering Hochtief wanted to assure all flanks of the PPP deal. We had to issue new pre-qualification documents, to assure consortium was equal, if not better, than the Jarvis one.'

'Technical due diligence had to be achieved, Hochtief FM worked to substitute Workforce FM, and banks had to look at the deal again,' he adds. 'While we started working on deal on December 2005, the actual financial close negotiations took 2 months.'

A source at Barclay's close to the deal said: 'The Bank had to work with the new bidder to achieve value for money by reflecting changes market terms and conditions since the Preferred Bidder announcement was made. Legal due diligence was difficult as new precedents from UK and Roads Contract were being adopted/enforced into the contract.'

'There were also significant time pressures and planning was running out - we had to complete 50 per cent of the site by December 2006 or planning could be revoked,' it added.

Both the Sponsors and Barclays, as arranger, worked with the client to achieve a deal meeting affordability and other contractual constraints. The partnership approach of all the parties was instrumental in bringing this project to a successful financial close.

'The result was a good deal, the client was satisfied with a unitary payment of around €7.6m (US\$9.1m) - even below Jarvis, due mainly to interest rates falling since after a few years,' O'Shea says.

Over the 25-year period, the contract will have an estimated total value of around €210m (US\$261.3m).

Conclusion

The scale of the troubles survived by the Cork School of Music PPP project is best exemplified by Irish Minister for Enterprise Trade and Employment Micheál Martin's comment at the formal signing of contracts in September 2005.

He said: 'The problems besetting the project were almost, appropriately enough, operatic in scope. However, at no time did I ever believe that it was going to be a tragic opera!'

Project manager Peter O'Shea says: 'That the project survived is good, that it worked after so many troubles and delays has merit. It was a painful learning curve, but a good one.'

For Hochtief, the purchase for a song of Jarvis' portfolio was undoubtedly a major coup, handing them access to the British Isles PPP markets.

And though some questioned Hochtief's logic at the time in acquiring the deals that had crippled Jarvis, the painless transition demonstrates that the risk paid off.

Interestingly, the deal also suggests that Jarvis' deals were not as structurally unsound as some commentators have suggested - though changing market conditions admittedly helped keep the Cork deal afloat.

Historians of the Jarvis' demise will still have to look to the core of the company, not its peripheries, to get a real sense of what went wrong.

Finally for the city itself, even if the deal was achieved late, the contract was agreed during Cork's term as European Capital of Culture and the new landmark public building will be part of its legacy.

The project at a glance

Project Name	Cork School of Music PPP project
Location	Cork city centre, southern Ireland
Description	The project involves the construction and facilities management for 25 years of a new, specialist music school for the Irish Department of Education and Science. The music school will have an area of around 10,500m2 and will accommodate up to 400 full-time and 2,000 part-time students.
Sponsors	Hochtief PPP Solutions (Ireland) Limited (50%); Barclays Private Equity (BPE) (50%)
Procuring authority	Irish Department of Education and Science
FM provider	Hochtief FM
Project Duration (Including construction)	25 years
Total Project Value	€72.7m (US\$86m)
Total equity	€7.6m (US\$9m)
Equity Breakdown	Hochtief €3.8m (US\$4.5m); Barclays Capital €3.8m (US\$4.5m)
Total senior debt	€65.1m (US\$77m)
Mandated lead arrangers	Barclays (sole arranger)
Legal Adviser to sponsor	McCann Fitzgerald
Financial Adviser to sponsor	David Wylde Project Finance
Legal adviser to banks	Arthur Cox
Financial adviser to government	Farrell Grant Sparks
Technical and commercial adviser to government	Gardiner & Theobald, Willis (insurance), Operis (model)
Date of financial close	5 September 2005

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