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OPTIONS CONCERNING THE NEW CONSTRUCTION

Document prepared by the Secretariat

I. INTRODUCTION

1. The present document is an updated and revised version of the document entitled "Options Concerning the New Construction", which was prepared by the Secretariat for the informal session of the Program and Budget Committee in February 2005 (document WO/PBC/IM/05/3). It integrates the information requested by Member States at that informal session on: (i) the possible financing of the new construction by the *Fondation des immeubles pour les organisations internationales (FIPOI)* (paragraphs 14 to 19), (ii) the economic justification for the proposed re-start of the new construction project as of 2006 in view of planned efficiency gains and other relevant considerations (paragraphs 32 to 39) and (iii) a comparison of the net present values (NPV) of the cost of the relevant financial options proposed in the document (paragraphs 27 to 30). The present document is aimed at being used by Member States as background information in the context of examining the proposal made by the Secretariat in respect of the new construction in the Proposed Program and Budget for 2006/07 (document WO/PBC/8/3, Program 31).

2. In September 2002, the WIPO Assemblies approved a project for the construction of a new administrative building and a conference hall for a total cost of 190.5 million Swiss francs (hereinafter referred to as "the Original Project") (documents A/37/2, A/37/9, A/37/10 and A/37/14, paragraphs 240 to 262).

3. In August 2003, following an international tender, a jury composed of representatives of WIPO Member States selected a general contractor: this general contractor was a consortium

composed of two parties. The Organization was obliged to terminate its contract with the consortium on January 12, 2004, because a dispute arose between the two parties, which prevented them from honoring their contractual obligations to WIPO.

4. In the meantime, an estimated income shortfall of over 80 million Swiss francs for the 2004-2005 biennium had become evident. In view of this situation, and following the termination of the contract with the consortium, the Secretariat considered it prudent to suspend the project and study alternative technical options designed to reduce its cost. It was also recognized that it would be a lower risk option for the Organization to maintain its reserves and explore the possibility of financing the new construction through external funding.

5. This document describes the alternative technical options (Chapter II) and possible alternative sources of financing (Chapter III). It also provides information on the tender and jury process (Chapter IV), and on the economic justification for the re-start of the new construction project (Chapter V). It also elaborates on the question of building *versus* renting (Chapter VI). Conclusions are given in Chapter VII.

6. When the Member States approved the Original Project in 2002, they did so after extensive analysis, including an independent evaluation report by the Swiss Federal Audit Office (i.e., the External Auditor) (document A/37/10). The decision taken at that time reflected the economic benefits of owning the new building *versus* renting office accommodation. The economic arguments supporting that decision remain as valid today as they were when the Original Project was approved. Chapters V and VI reiterate these arguments in light of the current (March 2005) financial circumstances.

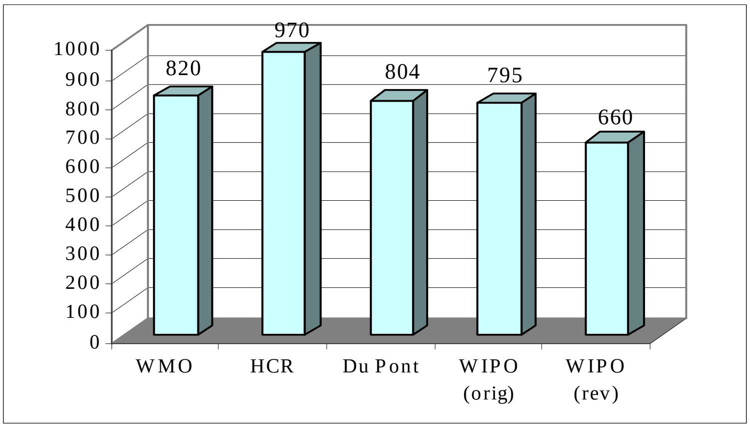
II. TECHNICAL OPTIONS

7. Following the decision to postpone the project, the Secretariat requested the architect responsible for the Original Project to study possible ways to reduce the cost of the administrative building which had been approved by the Member States in the framework of the Original Project. The outcome of that study is an alternative version of the Original Project with similar functionality (i.e., no decrease in the number of work places and parking spaces) but at a lower cost. This alternative project (hereinafter referred to as "the Revised Project"), would provide a five-floor, instead of six-floor, office building with the same number of work places (560) and parking spaces (280) as the Original Project. The main technical data of the Revised Project are shown below.

Number of work places	560	places
Cafeteria capacity	320	places
Underground parking	280	places
Gross surfaces		
Offices (1st to 5th floor)	13,364	m²
Common areas (ground, 1st floor)	4,251	m²
Technical areas (–1 level)	5,255	m²
Parking (–2 and –3 levels)	10,286	m²
Storage space (–4 level)	5,143	m²

8. As shown in the graph below, the cost per cubic meter of the Revised Project (660 Swiss francs per cubic meter) is lower than the costs of other corporate and United Nations agencies' buildings in Geneva, as well as of the Original Project (data extracted from the External Auditor's report, Table 8, page 17 of document A/37/10).

Cost Comparison by Volume of Various Buildings



(Sfr/m^3)

9. A technical and financial comparison between the Original Project and the Revised Project is provided in Annex I.

10. The total estimated cost of the Revised Project is 125.4 million Swiss francs, compared to 190.5 million Swiss francs for the Original project. A breakdown of the total estimated cost of the Revised Project appears in Annex II. As evidenced in that annex, the Revised Project would achieve a cost reduction of approximately 65 million Swiss francs by not constructing a new conference hall, eliminating the sixth floor and maximizing the number of work places in the remaining space, eliminating the *passerelle* with the Arpad Bogsch (AB) building, and revising certain technical concepts (for heating, air-conditioning and ventilation), as recommended by the External Auditor.

11. The Revised Project includes additional underground space for storage and/or parking in the area adjacent to the AB building. This space would provide extra parking facilities for a maximum of 260 cars, which could be also utilized by delegates and visitors. This means that the total number of parking places available could be, if required, 540[1]. The authorization to utilize this additional place as parking was delivered by the Geneva authorities in 2003.[2]

12. Including the cost of the purchase of the land (13.6 million Swiss francs), the total estimated cost of the Revised Project would be 139.1 million Swiss francs[3], of which 25.5 million Swiss francs, or 18.3 per cent, has already been disbursed (or committed) by

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[1] The additional underground space (6,100 m^2 parking + 2,250 m^2 liaisons = 8,350 m^2) was not included in the Original Project budget of 190.5 million Swiss francs. Therefore, additional specifications would need to be developed. The estimated cost of 8.9 million Swiss francs is based on the costs quoted by the general contractor in the 2003 tender and does not take into account possible discounts if a lump sum arrangement were to be made.

[2] In September 2002, the Member States had requested the Secretariat to study the question and contact the Geneva authorities with a view to ensuring the availability of these extra parking facilities (see document A/37/14, paragraph 262).

[3] This figure does not include the cost of purchasing the land (190.5 + 13.6 = 204.1 million Swiss francs).

WIPO. <u>In other words, the total remaining cost to be covered by WIPO, would be 113.6 million Swiss francs, as illustrated below</u>.

Description	Disbursed	Committed	Not Yet Committed	TOTAL
Office building	-	1.2	87.1	88.3
Additional underground space	-	-	8.9	8.9
Honoraria	5.8	3.5	11.4	20.7
Other costs	1.1	0.3	6.2	7.6
Purchase of land	13.6	-	-	13.6
TOTAL	20.5	5	113.6	139.1

25.5 million = 18.3% of total cost

III. FINANCIAL OPTIONS

13. Provided that the Revised Project, as described above, is agreed upon, there are three potential external financing options for its construction: (i) financing by the *Fondation des Immeubles pour les Organisations Internationales (FIPOI)*; (ii) a loan from a commercial bank[4]; and (iii) a lease arrangement with an investor-developer. All three options are discussed below. A comparison of the net present values (NPV) of future costs to WIPO under the bank loan (ii) and investor developer options (iii) is shown in Annex VI, together with the NPV of the cost of continuing the rental of certain premises. For the reasons explained in paragraphs 14 to 19 below, it does not appear useful to compare these NPV data with that of the *FIPOI* option.

<u>Option (i): Financing by the *Fondation des immeubles pour les organisations internationales (FIPOI)*</u>

14. A first option would be to finance the construction of the Revised Project through a loan from *FIPOI*. The statutes of *FIPOI* foresee the possibility of granting building loans free of charge to international organizations based in Geneva. *FIPOI* has always been a much-appreciated partner by WIPO. It has financed, namely, under very favorable conditions, the construction of the Arpad Bogsch and the Bodenhausen I buildings.

15. As soon as it became clear that the financing of WIPO's new construction project would neither be possible by means of the Organization's reserves nor by means of its operational budget, WIPO has established contacts with *FIPOI*. However, based on preliminary discussions and despite the undisputed architectural quality of the WIPO project, at this stage it appears not possible to determine, for the reasons enumerated below, whether and when *FIPOI* may be in a position to commit firmly to finance the WIPO project. Furthermore, even if *FIPOI* were able to commit itself to the project, the eventual costs to WIPO, including the foregone rental savings, could significantly exceed the project's current cost estimates.

[4] Different options would be available (fixed or variable interest rates, or a combination of both).

16. The first reason is that, as made clear by *FIPOI*s written communication dated January 6, 2005, as of early 2005, the Swiss Confederation had allocated all available funds for financing projects of this kind until the year 2007. Consequently, WIPO's request would only be considered as of 2008. Even then, the scale of the WIPO project is against it at a time when the Confederation is reducing its expenditure. In fact, the amount which would be requested by WIPO corresponds, on a yearly average, to *FIPOI*s entire fina ncing budget for four to five years.

17. The second reason is that, as also made clear by *FIPOI*, it would be necessary to ensure that the WIPO project meets the technical and financial criteria applicable to *FIPOI* financing schemes. To this aim, a request would need to be submitted to the head office of *FIPOI*, which would examine it from a technical and financial point of view. After having completed this financial and technical examination (from three to six months), the request would need to be submitted by the Head of the Federal Department of Foreign Affairs to the Federal Council and then transferred to the Federal Chambers for approval. It is estimated that this process may take anything from a year to 18 months. Bearing in mind the advanced state of the WIPO project and assuming a formal request for financing were to be submitted, *FIPOI* could either accept the project in its present state, ask for its revision, or reject it. In the event that the WIPO project were considered not to correspond to the Confederation's standards, significant additional costs and delays would have been incurred by WIPO.

18. The third reason is that the WIPO project may not be seen favorably when compared to projects from other institutions. As mentioned by the Swiss Delegation at the informal session of the PBC in February 2005, the current priorities of the Swiss government are projects in the areas of security as well as of humanitarian affairs. Also, WIPO is an income generating organization, unlike other competing organizations.

19. In view of the above reasons, the Secretariat considers that at this point of time the possibility of a financing by *FIPOI*is not realistic. Also, the potential loss of time and the risk of forfeiting past investments already made in the project could make the project too costly at the end. In addition, the opportunity cost of delaying the project implementation could be especially significant in view of the substantial rental costs that could be saved otherwise (25.8 million for three years and 43.0 million for five years).

<u>Option (ii): A Loan from a Commercial Bank</u>

20. A second option would be to finance the construction of the Revised Project through a loan from a commercial bank. A precedent exists in this regard as the Organization's Madrid Union building was financed by a mortgage from the Union Bank of Switzerland (UBS) in 1975. In constitutional terms, the possibility of WIPO contracting such a loan is not excluded by the WIPO Convention. The Secretariat has held informal discussions with a number of local and foreign commercial banks to explore the possibility of financing the construction by means of a commercial loan. Preliminary credit proposals have been made by two Swiss banks.

21. Based on these preliminary proposals, it would be possible for WIPO to obtain a loan covering the full amount of money yet to be disbursed to build the administrative building on the basis of the Revised Project (113.6 million Swiss francs). This would mean that the investments already made by the Organization in the project (cost of purchase of the land and the cost of the architectural study and its modifications), would be considered by the loan institution as a sufficient cash contribution on the Organization's part and no further cash

contribution would be required. The yearly estimated cost of such a loan would be 6.315 million Swiss francs (including interest and capital amortization) based on an interest rate of 3.56 per cent per annum[5]. The contractual arrangement between WIPO and the selected bank would have a duration of 30 years, which could be further extended, if required by the Organization.

22. Under such a scheme, the Organization would not be required to waive its immunity from jurisdiction or execution, except in case of a duly noted default[6]. Throughout the credit period the lending bank would abstain from demanding the constitution of a mortgage on the totality of the land and the administrative building provided that WIPO meet certain conditions. As mentioned by the Secretariat at the informal session of the Program and Budget Committee in February 2005, the original schedule of payments may be advanced if WIPO so requested.

23. The above financing option is shown in Annex III. <u>The amortization period would start only upon completion of the construction</u>, which means that during the construction phase (estimated duration: 26 months), there would be no amortization costs to be borne by WIPO. This means that during the construction phase the yearly cost to the Organization would be 1.846 million Swiss francs (at an annual interest rate of 1.5 per cent).

<u>Option (iii): A Lease Arrangement with an Investor-Developer</u>

24. A third option would be a lease arrangement with an investor-developer. An investor-developer, identified through a tender procedure, would finance the construction of the Revised Project and lease it back to WIPO. The initial minimum lease period would ordinarily be ten years. Subsequent to that initial lease period, WIPO would have the option to vacate the building, wholly or in part, or to buy the building at the initial project construction cost, in which case WIPO would need to identify the means to finance the purchase.

25. The estimated cost of this option is shown in Annex IV. If, as part of this arrangement, the investor-developer agreed to buy the land from WIPO and to reimburse to WIPO the expenditures incurred for the architect’s project, a certain amount of cash would flow back to WIPO (Alternative A). If the investor-developer did not agree to buy back the land and repay these costs to WIPO, WIPO would nevertheless receive from the investor-developer a yearly rent for the land and a cash flow back for the architect’s project (Alternative B).

26. The advantage of such an option would be that the responsibility of supervising and managing the construction process would shift from WIPO to the investor-developer. WIPO’s sole responsibility would be to ensure that the construction was carried out in accordance with the general tender.

<u>Relevant Net Present Value (NPV) Comparison of Options</u>

27. The comparison of the relative cost effectiveness of various options is provided in Annex VI. Discounted cash flows and net present values (NPV) are shown under the bank loan option, the investor-developer options (Alternatives A and B) and the option of

[5] Such as, failure to pay interest and/or principal within a period of 60 days following the due date, failure to abide by the so-called *pari passu* clause.
[6] The same process would apply in the case of the investor-developer option.

continuing to rent office spaces, instead of building ("rental option"). As explained above, the *FIPOI* option is not included in the comparison.

28. The information in Annex VI is shown by years numbered from 0 (current year) to 52 under Column C (last amortization payment under the bank loan option). It is recalled that, under the bank loan option, the loan amortization would commence only after the completion of the construction (2008 or year 3 in the Annex). In addition, Annex VI provides descriptions of the types of cash flows involved under each of the presented option, i.e. interest payments, loan amortization payments, purchase price or rental payments. The NPV of all future cash payments and receipts under the presented options are shown in Column A. These NPV values are considered good indicators of the cost effectiveness of various options which involve different cash flows and uneven time spans. Lastly, the relative cost effectiveness of the presented options is shown in Column B by way of indicating the percentages by which the least costly option differs from the other options.

29. As Annex VI shows, the bank loan option is financially more advantageous than the investor-developer options. In fact, the NPV of the bank loan option is 119.5 million Swiss francs, compared to 154.4 million Swiss francs under the investor-developer option (Alternative B) and to 158.9 million Swiss francs under the investor-developer option (Alternative A). In other words, the bank loan option is 29% cheaper than the Alternative B and 33% cheaper than the Alternative A of the investor-developer option.

30. For a comparison with the rental option, please see Part VI, below.

IV. TENDER AND JURY PROCESS

31. If all the necessary arrangements for the construction of the administrative building (by means of a commercial bank loan) fell in place, the Secretariat would launch a new international tender to select a general contractor. The final choice of the general contractor would be made by a special jury composed, as in the case of the 2003 tender, of representatives of Member States[i]. The timing of the new tendering process should ideally be such as to enable resumption of construction in January 2006, with February 2008 as the completion deadline.

V. ECONOMIC JUSTIFICATION FOR THE RE-START OF THE NEW CONSTRUCTION PROJECT

32. In 2002, when Member States approved the new construction, the prevailing view was that this approach represented the most economical use of the Organization's resources as opposed to renting premises. The Secretariat considers that this view is still valid, on the basis of the workspace, parking space and storage space requirements, which are described below.

Work Space Requirements

33. Annex VII shows year-end data on workspace requirements and availability, by individual premises, at WIPO, from 2005 through 2009. On the one hand, column A shows the total number of work spaces available at each given point in time in WIPO-owned premises (Sub-column A.1), and in WIPO-rented premises (Sub-column A.2). As Column A

shows, with the new construction, the total number of available work spaces would increase from 1,431 work spaces at the end of 2005, to 1,495 work spaces as of the completion of the new construction (2008). On the other hand, Column B shows the total number of workspace estimates to be required in the same period.

34. These requirements have been estimated on the basis of the number of WIPO employees, plus the employees of UPOV (to be housed by WIPO as per the WIPO-UPOV Agreement), and some additional 14 persons working for WIPO subcontractors on WIPO premises (security, restoration, travel agency, cleaning service, etc.). As shown in Column B, the Secretariat's current projections <u>(based on moderate growth of the registration systems in the medium term as well as accepted efficiency gains from the automation of the PCT)</u> anticipate a need for 1,500 workspaces by 2009, including a reserve of 100 workspaces. This projection is based on the fundamental assumption that the number of persons employed by WIPO in Geneva[7] will remain basically stable from 2005 to 2009 (average yearly growth of 0.7 per cent, or 10 new employees, having been allowed to cover, in a very conservative fashion, the expected growth of demand for PCT and Madrid services in this period, <u>this being understood that expected efficiency gains from the automation of the PCT will contain the number of PCT staff to the extent possible, despite a steady growth of demand for PCT)</u>. By proceeding with the new construction, this space requirement would be fully accommodated through the new administrative building and existing WIPO premises without the need to rent any other office space. This would represent significant savings (see Chapter VI for more).

<u>Parking Space Requirements</u>

35. Annex VIII shows year-end data on parking space requirements and availability, by individual premises, at WIPO, from 2005 through 2009. On the one hand, column A shows the total number of parking spaces available at each given point in time in WIPO-owned premises (Sub-column A.1), and in WIPO-rented premises (Sub-column A.2). On the other hand, Column B shows the total number of parking space estimates required in the same period. These requirements have been estimated on the same assumptions made for the workspace requirements.

36. As Annex VIII shows, with the completion in early 2008 of the Revised Project for the new construction, WIPO would have a total of 901 parking spaces in its own premises, for an estimated requirement of a little over 1,100 parking spaces.

37. This would enable the Organization to terminate the rental of almost all external parking facilities, except for a certain number which may be maintained in the *Parking des Nations*.

<u>Storage Space Requirements</u>

38. Annex IX shows year-end data on storage space requirements and availability, by individual premises, at WIPO, from 2005 through 2009. On the one hand, column A shows the total storage area available at each given point in time in WIPO-owned premises (Sub-column A.1), and in WIPO-rented premises (Sub-column A.2). As shown in Sub-column A.2, WIPO currently rents storage space at several locations in Geneva for a total area of 5,781 square meters. On the other hand, Column B shows the total estimated storage area

[7] Liaison Offices in Brussels, New York, Singapore and Washington excluded.

required in the same period. The lower requirements indicated in Column B from 2008 onwards are mainly due to planned introduction of movable shelves in the new construction, which will maximize the use of space and thus require less area for the same volume of stored items.

39. With the completion of the new construction in 2008, 5,143 square meters of storage space would be available. This may enable WIPO to discontinue rentals of storage space. It should be noted that the storage area in the new building would occupy a single underground floor in the -4 (lowest) level, which is not suitable for office use. The advantages of this arrangement include the savings of rental and transportation costs (0.5 million Swiss francs per year), improved security and thus reduced risks for the sensitive files safeguarded by the Organization on behalf of the users of WIPO's registration systems.

VI. BUILDING *VERSUS* RENTING: FINANCIAL ANALYSIS

40. The information provided in this document indicates clear advantages of building *versus* renting. As shown in Annex VI, the Revised Project under the bank loan option is estimated to be 75 per cent less than the rental of Procter and Gamble (P&G), CAM and *Nations* buildings. The savings, which would accrue to WIPO as it moves out of these rented premises, are estimated at around 90.1 million Swiss francs (difference between NPVs of rental option and bank loan option). Furthermore, the annual rental cost for these three buildings (which is estimated at 8.7 million Swiss francs) is significantly higher than the maximum annual cost of bank loan servicing of 6.3 million Swiss francs. It should also be noted that the annual cost of loan servicing would diminish each year as the loan principal is reduced.

41. <u>Finally, it is stressed that according to a recent market survey in Geneva, it would be impossible to find office space that meets WIPO requirements (number of work spaces, convenient location and cost-effectiveness), all of which are more attractive than the buildings currently rented by WIPO</u>.

VII. CONCLUSIONS

42. Based on the above, it is the Secretariat's view that it is in the Organization's best financial interest to invest in the construction of its own administrative building on the basis of the Revised Project, rather than continuing to rent office space. It is also the Secretariat's opinion that, of the options available, the most prudent and financially advantageous one is to finance this project by a loan from a commercial bank.

43. There are a number of financial advantages to such a solution:

(a) WIPO would become the owner of an asset the financial value of which is likely to increase over the years and which, if need be, could be rented out or sold;

(b) WIPO could capitalize on the investments already made in the project (25.5 + 1.5 = 27 million Swiss francs), including the international architectural competition process, architect's fees, and excavation;

(c) WIPO could take advantage of the favorable interest rates currently being applied in the capital market, the cost of which would be largely off-set by the interest received by the Organization on its monetary placements, as well as by the non-payment of rental costs; and

(d) A unified headquarters location would enable more efficient management, maintenance and security arrangements for WIPO premises as well as improved communication among the various WIPO services. Savings in security, management, internal communication and transportation would also be generated.

44. The Secretariat would issue a call for tenders to interested banks, with a view to signing a loan arrangement, before the end of 2005, with the selected bank. The WIPO Construction and Contracts Review Committee would make the selection. An independent expert would be engaged to advise the Committee on the best options in terms of interest rates and other technical conditions of the loan arrangement. Once the loan has been secured, and following the completion of a new tendering process for the general contractor, construction work could resume on January 1, 2006. The cost resulting from the above bank loan option has been integrated into the Proposed 2006-2007 Program and Budget which is being presented for the approval of the Member States at the present (April) session of the Program and Budget Committee.

[Annexes follow]

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[i] The same process would apply in the case of the investor-developer option.