Cover Note

The Government has reviewed the paper prepared by Messrs Mayor and Burchall. With the advice of its advisors, the Government has prepared the following response to the specific points raised by Messrs Mayor and Burchall (Commentators).

It should be noted that correspondence between the Ministry of Finance has taken place with both Commentators and at least one of them has been present at more than one seminar presented by the Ministry around the island. Many of the points they raise in this paper have been comprehensively addressed in prior correspondence. Moreover, invitations have been made to the Commentators to come to the Ministry of Finance so that the features of this transaction can be further explained. They have chosen, instead, to make public pronouncements on the project that totally ignore information already provided to them by Government.

The Government has retained several independent third party advisors in order to help assess the airport project, each with expertise in different disciplines and experience having worked on similar projects globally. This list of advisors includes:

- CIBC: CIBC's Infrastructure and Project Finance team has extensive experience in financial advisory for P3 projects. The team has closed over $15 billion in P3 transactions in Canada alone and has significant experience in working with a wide range of equity sponsors and construction contractors, both domestic and foreign.
- Bennett Jones (Bermuda) Ltd. and Bennett Jones LLP (Canada): Bennett Jones is an internationally recognized law firm and has experience in construction, project finance, complex cross-border and international transactions. It is one of Canada's leading public private partnership law firm.
- Leigh Fisher: LeighFisher is a management consulting firm with expertise in infrastructure advisory and consulting services. LeighFisher has over 65 years of experience in the aviation consulting sector and provides strategic facility and operational planning for their clients globally.
- HNTB: HNTB is an architecture, civil engineering consulting, and construction management firm with expertise in the aviation industry, including projects at the Denver, San Francisco, and Dallas Fort Worth international airports. HNTB understands the entire life cycle of infrastructure and provides services that solve technical, financial and operational challenges.
- KPMG (Bermuda) and KPMG (Canada): KPMG in Bermuda has a strong track record across a wide range of government and private sector work, including the King Edward VII Memorial Hospital P3 project. KPMG Canada is a leading financial and commercial advisor with global experience in public-private partnership and airport projects, including projects in Curacao, Bogota, Toronto, New York, and Hong Kong.
- Steer Davies Gleave (SDG): U.K.-based leading independent transportation consulting firm which specializes in preparing value-for-money reports.

The Commentators have no such expertise or experience. The tenor of their entire commentary starts from a position of “not” as opposed to, “how can we.” Their commentary and analysis is reverse engineered to lead to a predetermined conclusion. They propose no alternative plan, only criticize.

Their introduction stresses the downside risks that face Bermuda - particularly in tourism - but also generally. Everyone is entitled to his/her point of view, but purely negative strategic thinking and planning on the part of Government is not acceptable. The Government’s role is to lead its citizens forward not backward: - we must always be positive and have vision for Bermuda’s long term economic prosperity.

The challenge for the Government, particularly the Ministry of Finance, is to always be positive but at the same time protect against reasonably calculated downside risks. This is why we established the Fiscal Responsibility Panel and the Financial Policy Council to identify and shine a public light on the Government’s fiscal challenges and identify and analyze systemic financial risks, respectively.

The forecasts for traffic through the airport of the next 30 years are crucial to the financial viability of the project - but more importantly - it directly reflects our view of Bermuda’s future. In spite of the terrific figures this year for tourism air arrivals, up 14%, year to date, government has used conservative traffic forecasts to counterbalance the so called optimism bias.

The traffic forecasts (performed by British firm Mott Macdonald and peer reviewed by Leigh Fisher) calculate a 0.75% per annum growth in traffic for the next 30 years. This cannot be said to be unduly optimistic. There is also a numerically defined worst case scenario for each year in the 30 year projection. Any annual traffic performance that falls below that figure will trigger the Minimum Regulated Revenue Guarantee.

Hence, we are positive about our future but we are using a conservative traffic forecast for this financial model.

The Government has produced several analyses with the assistance of qualified third party advisors on the project and retained an independent third party firm (SDG) to perform an objective value for money assessment. The conclusion reached on all the analyses performed to-date is that the project does result in value for money for Bermuda.

The paper prepared by the Commentators contains a number of errors and presents a flawed analysis of the project. Specifically, this paper is premised on the following incorrect assumptions:

1. There is a minimum profit to Aecon; this premise is false. Aecon will be a shareholder of the project company Project Co. Aecon, along with other investors, will invest $65 million in Project Co and if the Airport does not perform well, Aecon could lose significant money on its investment.
2. Project Co has the ability to set fees as it chooses; this premise is false. The Airport Quango (the “Authority”), a wholly Government owned entity, regulates passenger fees and has discretion in approving increases in such fees.

3. Their presented standalone financial analysis is meaningful – false. As it does not compare the outcome to other scenarios such as Design Build Option or Retain Existing Terminal it is meaningless. Simply showing an option without any reference to any other scenario is very misleading and not market practice.
4. Their analysis focuses only on revenue and not on actual cash flows or net present value of the Project. This is not market standard practice. Market standard across all projects is to compare the net present value of all options and not the nominal cash flows.
5. Their analysis focuses on opportunity costs of options rather than on net cash flows of the underlying option – again not market standard practice.
6. Calculations made by the Commentators are compelling – false. They contain numerous errors which are outlined below.
7. Bermuda's debt capacity will be degraded as a result of this transaction as the project debt is payable by Bermuda - false. The debt is repayable only from the cash flows generated by the airport.
8. There is necessity to record a contingent liability on Bermuda's balance sheet – false. There is no need to record a continent liability on Bermuda's balance sheet in respect of the project as the liability of the Government is not both measurable and known as required under International Financial Reporting Standards
9. The project will not be a job creator – false. The project will result in new jobs for Bermudians and boost to Bermuda's economy

Overall, it becomes evident through the numerous errors and incorrect assumptions made by the Commentators that they lack the knowledge and experience in several areas and their conclusions are not credible. The Government retained several third party advisors with global experience such that these types of errors would not be made and that the correct conclusion would be reached.

A PRECIS OF A SUMMARIZED ANALYSIS OF THE PROPOSED DEAL BETWEEN AECON AND THE BERMUDA GOVERNMENT

A. On close financial analysis of all the financial figures put out up to 5th December 2016, the true cost of the ADA as currently proposed, will be around $1,395 million [$1.4bn]. This is significantly higher than the figure currently put out by Government.

   The $1.4bn figure does not represent the cost of the project to the Government and it contains various calculation errors. Further details are provided in Points 49 to 57.

B. If this ADA is consummated, the Government will commence a process of revenue surrendering which will immediately increase the size of Government's deficit, which, in turn will mandate an immediately higher rate of borrowing by Government.

   The transaction has been structured with the assistance of expert financial advisors to specifically avoid an increase in the Government's cost of borrowing. The prediction that the transaction will lead to an immediate increase in the Government's interest rate is unfounded.

C. The downside risks, in particular, the levelling off or decline of future Leisure Tourist Air Arrivals, are real. These downside risks are not referred to at all in Aecon's future forecasts for revenue from the Airport.

   Both Aecon and the Government independently retained professionals to develop a robust traffic forecast. Specifically, the traffic forecast which underpins the project has been developed by an internationally recognized firm with expertise in preparing airport traffic forecasts and master plans. Furthermore, this forecast was peer reviewed by an independent firm and found that the forecasts was prepared using reasonable assumptions of the future based on what is known today. There is no higher degree of assurance that Bermuda could obtain with respect to the traffic forecast. Both Aecon and Bermuda are relying on the traffic forecast.

D. If downside events occur, the Government will be locked into a requirement to dip into its depleted [by revenue surrendering] revenue stream and make good any losses below the 'base case' level so that Aecon and its shareholders will always have a year-end profit.

   This statement is incorrect. The minimum revenue guarantee funds paid by the Government can only be paid to lenders in the event there are insufficient net cash flows generated by the project to pay debt. No guarantee money is ever paid to the equity investors and there is no minimum profit to Aecon. It is important to note that the deal was specifically structured to avoid this.

E. Under this proposed ADA, Aecon/new Quango will have the right to increase all Departure Taxes, all landing fees, all rents to all concessions and any other fees. Should Aecon/new Quango not have the particular right to raise any one particular fee/tax; Bermuda's central Government will be obliged to do so in order to maintain profitability for Aecon.

First, to correct the terminology, Project Co will be operating the airport and the Authority (referred to a "new Quango") will be the Government body charged with overseeing operations and providing Retained Government Services. Second, there is no minimum profit concept for Project Co or for Aecon as Project Co's shareholder. Third, the majority of fees are regulated by the Authority and the Authority, in its sole discretion, approves changes in fees. Neither Project Co nor its shareholder, Aecon, has the power to increase regulated fees as it chooses. Fourth, there is no facility to allow the central government to increase fees to maintain profitability.

F. For the full thirty-three years and four months of this proposed Agreement, Aecon will be exempt all payroll taxes, other taxes, customs duties, and other fees and licences normally levied on companies [including IB companies] that are operating in, and have a labour footprint in Bermuda.

First, the term is 30 years and not 33 years and 4 months. Second, the Government routinely provides broad tax exemption incentives for foreign investment of this nature such as hotel developments. Third, this is a net neutral item from a tax perspective as the Government is not currently generating any tax cash flows from the airport today as it is a government owned entity. In fact, even if the airport was procured using the traditional procurement methods the relief would still have been provided. It would have made little financial sense for Government to charge Customs Duty and other taxes on a Government project. It is also important to note that there are broader tax implications to the economy through increased passenger travel and an increase in hotel accommodation taxes which have not been addressed by this paper.

G. Aecon will actually borrow any funds that are needed. However, regardless of how many 'Special Purpose Vehicles' are inserted or created and set between lenders and borrowers; the Government will always carry the risk of having to repay the borrowed funds. i.e. Bermuda taxpayers will always be the final guarantors of any Debt that is taken on by Aecon, Project Co, or any other SPV created by the Government.

Bermuda will not need to step in and repay the debt as the debt is backed solely by the cash flows of the airport. Bermuda will not need to repay the borrowed funds unless Bermuda defaults in the performance of its obligations or elects to terminate the Project.

H. The Government of Bermuda will therefore acquire a 'contingent liability' that is real and that must be reflected in Government's accounts. Not to reflect this contingent liability would be to account for funds much as Enron or Bernie Madoff were wont to do.

This statement is incorrect. The Government is providing a Minimum Revenue Guarantee to Project Co. in order to ensure efficient private financing and to reduce the cost of borrowing. According to the Government's accounting advisor, as the occurrence of the future confirming event (for the need for Government contribution) is not yet determinable, the existence of the Minimum Revenue Guarantee should be disclosed in the Notes to the Government's financial statements. No amount of contingent liability will be reported on the balance sheet until the confirming event becomes likely. This is similar to the treatment by the Government of the BHB guarantee which is not included on the Government's balance sheet, unless the guarantee becomes due and payable by the Government. All guarantees are disclosed in notes to the financial statements of the Consolidated Fund.

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COMMENT AND OBSERVATIONS ON THE AIRPORT DEVELOPMENT AGREEMENT AS AT DECEMBER 6th 2016]

General Overview.

1. Aecon/Quango gets exclusive 30 year rights to run Bermuda's only airport terminal.

   First, Aecon/Quango is an odd term. The Commentators appear to be confused about the structure of the parties to the contract. Aecon will be a shareholder in Project Co. Project Co will operate the Airport. Quango is the Authority, a government entity that will provide Retained Government Services and will oversee the project. "Aecon/Quango" does and will not exist. Second, this term of the concession is consistent with airport concessions as well as private public partnerships in Canada and around the world. For instance, most concession terms are construction term plus 30 years. The Government actually negotiated a better deal and restricted this to just 30 years with no extensions. Third, with regard to exclusivity, this is a standard provision that is included in all assets of this nature. For instance, lenders, and equity investors, would not advance funds to a project if another party could simply build another airport in Bermuda which would result in a deterioration of cash flows and them losing their money.

2. Aecon/Quango keeps all the money from unregulated fees and gets money from the regulated fees

   As noted above, "Aecon/Quango" is not an entity. Project Co retains all the revenue from the airport. This is standard provision in airport concessions globally. The funds received from

these fees are used to operate and maintain the airport, finance the construction of the airport, as well as repay lenders and equity investors.

3. Aecon/Quango can set prices and fees. Aecon/Quango can charge whatever they want for some fees (e.g. "Airport Improvement Fee", landing fees,…)

   As noted above, "Aecon/Quango" is not an entity. This statement is inaccurate and does not reflect the terms of the deal. All aeronautical fees (e.g. Airport Improvement Fees, landing fees, etc.) are regulated by the Authority. Specifically, Project Co cannot increase fees above inflation without express consent of the Authority which can be granted or withheld at the discretion of the Authority. As a result, Project Co does not set fees and prices and they cannot charge whatever they want.

4. If the revenue from regulated fees fall below a 'base case', then the Government must pay and make up the difference.

   Bermuda will pay funds into a segregated trust account for the benefit of lenders if passenger volumes are below a certain threshold which is set at a level far below base case traffic levels. If regulated revenues are below the base case level, but above the threshold for payment, then no payment would be required. If net cash flow from the airport is insufficient to pay the debt payments to the lenders, funds from the segregated account would be applied to make payment to the lenders.

   It should be mentioned that while the Government is providing some support for the downside, the Government is sharing on the upside also. There is a 50% sharing of the upside provided to the Government if the project performs better that predicted.

5. If Aecon isn't making "enough" money, because its operating costs are higher than budgeted for, then, under the Revenue Guarantee, the Government will make payments to increase Aecon's Cash flow.

   The statement above is false. For clarity, the revenue guarantee is for the sole support of lenders and not Project Co or its shareholders. No cash flows from the revenue guarantee can ever flow to Aecon/Project Co as the funds can only be paid into a segregated account for payment to the lenders. Second, if the revenue guarantee is triggered, then Project Co is making no money as there is insufficient funds to pay dividends to equity. Third, as the name indicates, this is a revenue guarantee only. If operating expenses are higher than anticipated, but traffic volumes are above the revenue guarantee threshold, no payments are required.

6. For the 33 year duration of the planned process, Aecon cannot be taxed on anything; thus Aecon never ever becomes a part of Government's tax base.

   First, term is 30 years and not 33 years and 4 months. Second, the Government routinely provides broad tax exemption incentives for foreign investment of this nature such as hotel developments. Third, this is a net neutral item from a cash flow perspective as the Government is not currently generating any tax cash flows from the airport today as it is a

government owned entity. It is also important to note that there are broader tax implications to the economy through increased passenger travel and an increase in hotel accommodation taxes which has been conveniently excluded from this paper.

7. Aecon is going to borrow the money. The simple insertion of *Project Co?* between the foreign lenders and the on-Island borrower of last resort is simply a way of hiding, or attempting to hide, a significant slice [$270 million?] of national debt inside a special-purpose entity. It is an off balance sheet financing mechanism popularized by Enron.

   This is the predominant financing structure used globally. For clarity, Aecon is not the borrower and the debt holders have no recourse to Aecon or Bermuda. The debt is only backed by the underlying cash flows of the airport. Government is not a "borrower of last resort," if there is such a thing, neither is it hiding anything.

8. In providing a Revenue Guarantee ensure Project Co has sufficient annual cash flows to service its debts and maintain an investment grade rating for the bonds, the Government retains most of the financial risk for repayment of the bonds. .

   Bermuda is not guaranteeing the debt and only making discrete payment to lenders in the event traffic volumes are far below historical levels. The majority of financial risk does not sit with Bermuda, but rather with Project Co.

9. That contingent liability will be described in Governments Financial Statements. This contingent liability will impair Government's financial strength and weaken sovereign its Credit Rating. This accounting and liability reality runs contrary to all Government statements which regularly say that there will be no increase in National Debt or associated obligations.

   The statement is false. The Government is providing a Minimum Revenue Guarantee to Project Co. in order to ensure efficient private financing and to reduce the cost of borrowing. According to the Government's accounting advisor, as the occurrence of the future confirming event (for the need for Government contribution) is not yet determinable, the existence of the Minimum Revenue Guarantee should be disclosed in the Notes to the Government's financial statements. No amount of contingent liability will be reported on the balance sheet until the confirming event becomes likely. This is similar to the treatment by the Government of the BHB guarantee which is not included on the Government's balance sheet, unless the guarantee becomes due and payable by the Government. All guarantees are disclosed in notes to the financial statements of the Consolidated Fund.

   The Government's financial advisor has provided their views that the contingent liability will not impair Government's sovereign credit rating.

10. In establishing or setting up an Airport Quango to interface, and interface permanently, with Aecon; Government will surrender – lose - one or more revenue streams. This will happen so that the new Quango will have a revenue stream large enough to fund Aecon to the level that is contracted between the Government and CCC/Aecon or whoever is designated as the receiver of funds that are intended to compensate the 'developer'.

There is no revenue stream arrangement between the Government and CCC/Aecon. The Government will allow Project Co to receive all of the revenue from the Airport, subject to Project Co paying all the costs of building, operating and maintaining the Airport. The Authority will only have revenue that it can derive from the exploitation of the assets that are being transferred to it by the Government for the purpose of providing Retained Government Services. The Government will retain the obligation to fund the provision of Retained Government Services by the Authority, a subset of its current funding obligations to operate the Airport.

<u>Government deficit will increase and Government must increase National Debt by borrowing.</u>

11. The surrender of a significant slice of Government revenue [$37m would be 3.7% of revenues projected for 2016/17] will immediately impact and degrade Government's current 'revenue short' [deficit] position. Government revenue would reduce from $996.9m to $959.9m.

    The government generated $3.4 million of net cash flows from the airport in 2015/2016 which excludes capital expenditures for maintenance and repairs to maintain the aging infrastructure. After factoring in the required maintenance capital expenditures, the airport actually generates negative cash flows and this will only increase as the required maintenance capital expenditures increase over time. It is only the net revenue that is transferred. Looking simply at revenues is a very poorly constructed analysis and does not paint the full picture. Furthermore, the capital expenditures to maintain the terminal will only increase over the next several years which will only increase the current net cash outflow from the airport.

12. Government's parallel passing on of all Airport related expenses to the new Quango currently amounts to about $10m. This expense passing over immediately reduces Government's expense profile. In Government's 2016/17 spending plan, this would reduce Government's planned spending on expenses from $1,196.3m to $1,186.3m. However, given revenue reduction, the deficit would rise from $199.4m to $226.4m. This reflects the $27m net revenue surrender. The table shows this. *[Revenue/Spend figures are from Budget 2016/17.]*

THE FINANCIAL IMPACT OF THE CURRENT AIRPORT FINANCING DEAL			
	TYPICAL NOW		TYPICAL LATER
	PRE-AECON		POST AECON
REVENUE	$ 997	Government surrenders $37m Revenue	$ 960
LESS EXPENSES	$ (1,196)	Government surrenders $10m Expenses	$ (1,186)
Government's Deficit	$ (199)	Government's deficit increases	$ (226)

The Commentators' analysis misses several cash flows that need to be included. In particular, the analysis does not include the transfer of capital expenditures. In fact up-front cap-ex

costs required to make urgent near term repairs to the existing terminal as well as some improvements to the facility that are necessary to continue operations were estimated by GOB's technical advisor to be $62.3 million in repairs and $104.8 million in improvements in a 2013 report. In addition ongoing maintenance costs need to be also included.

The Commentator's analysis also does not include the net savings to the Government of $1 million for central Government costs no longer paid for by the Government and transferred to Project Co.

It should be noted that the above excludes the potential for the Government's 50% sharing in the upside of the project. The broader economic and tax benefits of the project are also not included. Hence the Government's deficit increase as suggested by the Commentators is significantly overstated.

13. In full context, when the revenue surrender and expense passing over are set side-by-side, Government ends up with an increase in its deficit. This deficit can only be funded by more additional borrowing. This requirement for added borrowing is driven specifically and only by the overall net revenue surrender of former DAO revenue to Project Co. It is therefore completely incorrect to say or suggest that Government will NOT add to the National Debt if the ADA is signed and this scheme progresses as currently planned. *[See paragraphs 49 to 61 for a more thorough and detailed analysis of the financial factors]*

As noted in point 12 above, the commentators' have miscalculated the impact on the deficit.

Power to raise or increase taxes is handed over to a for-profit private corporation

14. If Government has to pay funds to the new Quango in order that it can compensate for reduced cash flow under the base case scenario, then as long as Government spending is in a deficit position, this payment will also immediately further increase the size of the net revenue surrender.

Bermuda does not simply compensate Project Co (not the Quango) if cash flows are below the base case forecast. The actual way it works is that Bermuda would pay funds into a segregated trust account for the benefit of lenders if passenger volumes are below a certain threshold which is set at a level far below base case traffic levels. If regulated revenues are below the base case level, but above the threshold for payment, then no payment would be required.

15. Taking 2015/16 as a typical year, there were about 220,000 Air Visitors to Bermuda and Bermuda's residential population was about 61,750 *[Government has reported (in the Bond Prospectus for the $665m Bond issue that is currently underway) that 2015's ResPop was 61,735. There is a mini-Census underway. The results are not likely to be ready until Jan/Feb 2017. But this mini-Census should/will confirm that Bermuda's 2015 ResPop is LOWER than Bermuda's Census 2000 ResPop of 62,059.]*

The traffic forecast takes into account factors such as Bermuda population growth and its impact on traffic. As part of the forecast, the traffic forecast assumes that the long-term population of Bermuda will slightly decrease over the 30 year concession term. Specifically, population forecasts were derived using data from the Department of Statistics.

16. Currently, about 60% of Airport revenues generated from Departure Taxes are paid by Air Departing Visitors; and 40% by Bermuda residents making multiple flights. In 2015/16 this amounted to about 220,000 visitors and 138,000 Bermuda residents. This was the makeup of the 358,000 persons who paid the $50 a head Departure Tax providing $17.9m in total paid in to the Tax Commissioner, in 2015/16. Of this $17.9m, $10.9m was derived from Visitors and $7.0m from Bermuda residents.

    Majority of airport projects globally are financed through passenger fees. This has been benchmarked through numerous examples and confirmed with the Government's third party technical advisors.

17. From the above, Bermuda residents would appear to travel at the rate of 2.3 transits per resident per year. However, the segment that generates the greater multiplicity of trips is the International Business [IB] segment. It is unknown what percentage of those 138,000 transits are IB persons; but it is likely that about 90,000/105,000 [65%/75%] are by IB personnel; with other Bermuda residents producing the remaining 48,000/33,000 [35%/25%] of transits. Essentially, this is a hidden tax increase on IB personnel who are the majority of multiple travelers; and on traveling Bermudians.

    Majority of airport projects globally are financed through passenger fees. There would be no difference under any procurement scenario. It is also important to note that this Project is supported by passengers, 40% of whom are Bermudians and 60% of travelers are foreign. By way of comparison, the hospital project is borne 100% by Bermudians/residents.

18. Going forward, under the scheme as currently planned, it is intended to impose several other new and additional fees on each transiting passenger. Thus 40% of any new fees will be borne and paid by Bermuda residents. These new fees will have exactly the same impact as would general taxes increased or new taxes imposed by Bermuda's central Government.

    There are no new fees being contemplated, so point about "several new fees" being introduced is incorrect. Furthermore, as stated earlier, the Authority has discretion in approving increases in fees.

19. It is clear that now and going forward, at least 40% of all revenues raised through passenger activity at Bermuda's Airport will be paid in by Bermuda residents. Hence the arguments that 'others' will pay is only 60% correct; or might be considered to be 40% wrong. Bermuda residents and Bermudians will contribute directly and specifically to all revenues that will be surrendered to Aecon/Project Co. Under current plans, new or increased taxes or fees can be levied by Project Co whose primary objective is to keep cash flows high so that Aecon is kept in

profit. <u>This is a clear derogation of some central government power to a privately held for-profit business corporation.</u>

Passenger fee increases in excess of inflation and certain specified costs items must be approved by the Authority. Second, all airport transactions globally are financed, to some degree, by increased passenger fees and this is common market practice.

<u>Tourism projections made by Aecon and Tourism's future, in general</u>

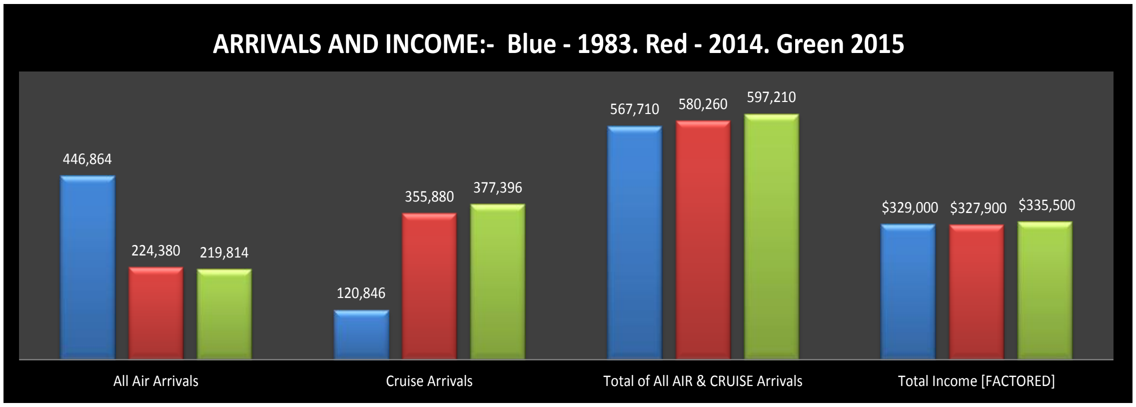
20. The Aecon analysis and forecast of future Leisure Tourist Air Arrivals is only partly complete. It is also heavily biased because it shows only a completely rosy future. There is no allowance whatsoever for a levelling of Leisure Tourist Air Arrivals There is no allowance whatsoever for a further decline in Leisure Tourist Air Arrivals. *[Important note: each Air Arriving Tourist becomes an Air Departing passenger who pays Departure Tax.]*

Aecon is contributing significant equity ($65 million) and investing on the basis of an increase in Leisure Tourist Air Arrivals. Aecon loses money or earns sub-optimal returns if leisure tourist air arrivals do not increase and as, contrary to the commentators'' understanding of the deal, there is no minimum profit to Aecon. Furthermore, as discussed earlier, the traffic forecast has been prepared by experienced professionals in traffic forecasting and, based on an independent peer review, it was concluded that the assumptions used were reasonable. As a result, the claims noted by the commentators are simply unfounded.

21. If Leisure Tourist Air Arrivals do level off or decline from current levels, then according to the 'base case' proposals as currently set out, the Government will have to pay in additional funds in order to close the revenue or cash flow gap and thus preserve Aecon's guaranteed profit.

There is no guaranteed profit to Aecon and the deal was specifically structured such that no funds from the revenue guarantee could ever flow to equity investors. Aecon is contributing significant equity ($65 million) and investing on the basis of an increase in Leisure Tourist Air Arrivals. In fact, they lose money or earn suboptimal returns if this does not happen so they have a large vested interest in ensuring that leisure tourist air arrivals increase.

22. Historically, Bermuda was a premier Land Destination with 85% of its Leisure Tourists coming by air and only 15% of Leisure Tourists coming by cruise ship. This was a ratio of six Air to one Cruise. In 2003, that changed. It became one Air to one Cruise. By 2015, the ratio had changed further. In 2015, five came by Cruise for every two who came by Air. Numbers? 377,000 by Cruise and 140,000 by Air. *[The chart figures are provided by the Department of Statistics in their Quarterly Bulletins of Statistics.]*



The reason why Bermuda has had difficulties in maintaining the image as a premier land destination is the quality and number of hotel inventory where investment has not been made over the past few decades. This was noted as the primary driver of increasing inbound vacationers by independent consultants. Specifically, Bermuda is a luxury destination, with luxury pricing, which must have commensurate hotel accommodation and this has not been the case. There has been significant investment in hotel stock in the past few years as well as new, high quality hotels coming online which will help improve inbound vacationer volumes.

23. Hence, it is clear that in 2015 and going forward Bermuda is heard of, seen, advertised, marketed, sold, and above all else bought and paid for, as a cheap Cruise Destination rather than a premier and expensive Land destination.

Per the previous comment above, this statement is inaccurate and does not appropriately characterize the situation. Bermuda is still seen as a high quality, luxury land destination; however, it is important to ensure the hotel stock, both in terms of quality and number, matches this image. The significant investment in hotel stock over the past few years by such entities as the Hamilton Princess helps solidify this image.

24. Each Cruise Arriver spends less than each Air Arriver. The ratio is a nickel and a dime by each Cruiser for every dollar spent by each Air Arriver – regardless of whether Business Visitor, Family & Friends who are visiting on-Island family and friends, or Leisure Tourist.

This point is moot as this project as well as other government initiatives with respect to new hotel developments is aimed at driving increases in air passengers. The purpose of this project is not related to cruise passengers.

25. Income from Bermuda's Tourist industry overall is lurking in the $329m to $375m range. This low Tourist income and relatively high Tourist numbers indicate an Industry that has changed radically, and that is not growing, but is just hanging on. In addition, it has to be recognized that since 2010, Tourism has been subsidized. In 2016, Tourism is subsidized with Payroll Tax, Hotel Tax relief, and Air Seat Guarantees to several airlines.

As noted earlier, the industry has not been growing due to the historical lack of investment in the hotel stock with Bermuda being a luxury end destination. With recent hotel investment

by such firms as Fairmont and new hotel developments coming on line in the next few years, there should be significant growth in tourist numbers.

26. All good analyses show that while Bermuda's overall Visitor numbers stay relatively high *[since 2004, between 500,000 – 650,000],* Bermuda's Leisure Tourist Air Arrivals have been steadily trending down since 1987. Cruise Arrivals have compensated by steadily trending upwards. This is clearly shown by the chart which shows the trends in Tourist numbers over 32 years.

    The point raised here does not actually go to the heart of the problem which is the quality and number of on island hotel stock. There is a proven and direct correlation to the quality and number of the hotel stock on the island and inbound air travelers. Recent government initiatives regarding hotel developments and investment made in hotels on the island are in an effort to drive improvements which statistically lead to higher inbound vacationer volumes.

27. Aecon's forecast envisages up to a 25% improvement in Leisure Tourist Air Arrivals between the end of their Airport development and 2023. Why and driven by what global and well as on-Island factors would that happen? Why would a thirty-two year decline suddenly metamorphose into a sudden six year rise? Aecon provides no answers. Aecon simply projects a rosy future.

    Please see notes above about hotel stock inventory and correlation with inbound passengers. Also, Aecon is contributing significant equity ($65 million) and investing on the basis of an increase in Leisure Tourist Air Arrivals. In fact, they lose money or earn suboptimal returns if this does not happen so they have a large vested interest in ensuring that leisure tourist air arrivals increase. There is no benefit to them forecasting a "rosy" picture as they lose money if it does not materialize.

28. Changes in Business Visitors and Family and Friends visiting family and friends are dependent on the state of business in IB and the number of people living on-Island. If Leisure Tourist Arrivals level off and stay in the doldrums of 120,000 to 150,000 for the next decade, the inevitable shortfall or levelling off in Airport revenue from Leisure Tourists arriving by air will have to be consistently made good by a Government that has surrendered streams of Airport revenue to a new Quango/Aecon.

    There is no requirement for the Government to "make good" airport revenue shortfall from Leisure Tourists, other than the Minimum Revenue Guarantee explained previously.

29. Given the near future likelihood of nearby Cuba becoming a massive Leisure Tourist attraction; given the continuous improvement/advances made by the huge and hugely profitable world-wide Cruise ship industry; the entire globe is becoming more easily accessed and above all else more affordable for ordinary men and women.

    Bermuda is not competing for the same tourism travelers that will visit Cuba. Cuba is a low end, inexpensive destination which is marketed to budget travelers. Bermuda is a luxury destination with high end pricing, so there will be little leakage of passengers from Bermuda to Cuba from an air passenger perspective. This was clearly noted by Bermuda's traffic consultant which is an international firm with experience in traffic forecasting.

30. The clear Aecon/new Quango plan to steadily increase the cost of all air travel to and from Bermuda is specifically and clearly a plan that runs counter to all current and likely future changes and advances in global leisure travel. In the shark-eat-shark global free market, the rest of the globe is price and cost-cutting to get business. However, Aecon's plan and way forward is to specifically build in future higher costs to all air travel to and from an already expensive-to-get–to Island; and an Island which is currently, aggressively, and successfully being marketed as well as purchased as a cheap Cruise Destination.

There is no evidence of airports and other destinations cutting passenger fees and actually the opposite is true. Airports globally are continuing to increase their passenger fees in order to invest in their airports and improve the quality of service.

31. Aecon's forecast and analysis for Bermuda's Leisure Tourism is incomplete. Its lack of any reference whatsoever to flat-lining or declining Air Tourist figures verges on being completely dishonest. Its total ignoring of any downside is highly ir-regular for any honest business organization. It reminds of the rosy revenue scheme so successfully perpetrated, for so many years, by the now jailed Bernie Madoff.

Comments like this confirm the absence of objectivity and professionalism of the Commentators' paper. Both Aecon and the Government independently retained professionals to develop a robust traffic. Specifically, the traffic forecast which underpins the project has been developed by an internationally recognized firm with expertise in preparing airport traffic forecasts and master plans. Furthermore, this forecast was peer reviewed by an independent firm and found that the forecasts was prepared using realistic assumptions of the future. There is no higher degree of assurance that Bermuda could obtain with respect to the traffic forecast.

32. <u>The future of Leisure Tourism to an expensive Land Destination, which, in the global market is what Bermuda is, is highly problematic. It requires far more study and consideration than the incomplete treatment that is displayed in the Aecon documents supporting Aecon's proposal and Aecon's determined effort to lock-in a guaranteed profit for the next 30 years.</u>

First, there is no guaranteed profit for Aecon. Second, there already have been significant studies performed on traffic by two internationally recognized traffic forecasting firms with decades of experience forecasting traffic. Third, recent initiatives by the Government to improve investment in hotel development will lead to an increase in inbound vacationers and this is statistically supported by empirical evidence. Fourth, Aecon is investing significant capital into the project and will lose money if the traffic forecast does not materialize, so there is no reason for them to paint this so called "rosy picture" alluded to in this paper. Fifth, the 30 year term of the concession is not an outlier for P3's. The KEMH P3 contract is for 30 years.

<u>Jobs, jobs, jobs</u>

33. One of the primary and strong political and economic reasons advanced for this CCC/Aecon new build was that it would provide jobs for hundreds of Bermudians. In March 2015, in a Town Hall meeting in St Georges, the Minister for Finance said that the project as proposed

would provide around 600 new jobs with 75% for Bermudians [450 new jobs for Bermudians] and 25% for Canadians [150 new jobs for Canadians]. In a November 2016 paper prepared for Parliamentarians, the Minister for Finance said that the anticipated provision of new jobs would be 400 but now with 60% Bermudian [240 new jobs] and 40% Canadian [160 new jobs for Canadians].

The project will generate significant local construction jobs for Bermudians. Not proceeding will generate no jobs.

34. The November 2016 new jobs promise shows a 47% reduction in job opportunities for Bermudians. However, at the same time, job opportunities for Canadians increased by 7%. This is a completely unhealthy and huge imbalance in the promised growth of new job opportunities for Bermudians.

There have been extended discussions with Department of Workforce Development on the skills available locally. The number of jobs being created has been refined as the negotiation/planning/consultation process has moved forward. Also, the Commentators have conveniently dismissed the intern and training opportunities that will be created by this project.

35. As a profit-seeking business, and under the terms set out in the proposed ADA, Aecon/new Quango will have no contractual requirement to provide a certain or fixed percentage or quantity of jobs for Bermudians. Therefore the post-build 30 year operators of the Air Terminal building can have a workforce that is as easily 80% Canadian as 80% Bermudian. There is no safe-guarding of jobs for anyone – particularly for Bermudians.

This is, again, non-objective speculation indicating the unprofessional nature of the Commentators' paper. For the operations of the airport, Aecon has made employment offers to all current staff at Department of Airport Operations. This demonstrates Aecon's commitment to employ Bermudians. As agreed with the Government, the employment offers must be no less favourable than current employment terms.

Economic stimulus to Bermuda's economy.

36. One of the strong and realistically achievable political and economic arguments for this project being a PPP or P3 project was that it would provide a major stimulus to Bermuda's economy; with this stimulus coming from $267 million in 'direct inward investment'. However, given all the publicly disclosed information thus far, it becomes evident that the economic stimulus impact will be low to small.

Beyond the direct economic impact of the construction spending, the project will contribute to Bermuda's attractiveness as a tourist destination and business centre.

37. First – as for all new construction work in Bermuda, all materials used in the construction/new build will be imported. Hence the $100m or so that represents the cost of materials will never have a direct impact on Bermuda's GDP. That $100m or so spent on materials will be spent in Canada. It will therefore boost Canada's GDP, Bermuda's.

- Second – With a 40% Canadian workforce, a significant chunk of labour costs, perhaps as much as $30 million will not be spent here in Bermuda, but will be sent home, as savings, to Canada.
- Third – The proposed new build will be phased over 40 months [Aecon's time projection]
- Fourth – Any economic stimulus will come from wages paid to the Bermudian labour component; and from direct spending with Bermudian sub-contractors who would, necessarily, have to have 100% Bermudians workforces; else there would be a further 'bleeding' out and loss of local spending from wages paid by sub-contractors.
- Fifth – the best estimate for the final impact of $267 million of 'direct inward investment' is that only about 35% - 40% of that $267m will directly impact Bermuda's GDP during the 40 month new build phase. This would be something between $95m and $110m going directly into Bermuda's economy; thus having a direct impact on Bermuda's GDP.
- Sixth – When spread over 40 months, this works out to direct on-Island stimulus spending that is between $29m a year and $33m a year – about $2.5m to $3.0m a month.

These points are meaningless as they would apply to virtually any major project in Bermuda which would undoubtedly involve the importation of materials and the use of specialized labour from overseas. It is just the nature of a small island that produces very little in terms of physical products. The project will generate positive impact to Bermuda, specifically for Bermudians employed in the construction industry. Perhaps if the Commentators were unemployed construction workers their perception of this Project might be different.

38. Considering the depth and length of Bermuda's recession, this relatively small stimulus will help. However, it will not, on its own, provide any sizeable or easily noticed stimulus to Bermuda's national economy. And, certainly, Bermuda will never receive the economic stimulus from the on-Island spending of the $160m - $175m (or so) that will be spent in or sent to Canada. This because Bermuda and its economy will only ever feel the impact of about 35% - 40% of that $267m 'direct inward investment'. The remaining 60% - 65% of 'inward investment' will actually be dissipated overseas.

    Given the industries, labour, and natural resources available in Bermuda, it is expected that imported supplies and services will be a significant component of project capital costs. Nonetheless, the project will still provide a positive contribution to the economy and significant opportunities to many Bermudians. The positive effect it may have on Canada's economy will clearly not be material to that country's overall macroeconomy. It doesn't take very much to have a material positive impact on Bermuda's, and this project will do that.

39. However, under this proposed PPP/P3, Bermuda's economy will be required to pay back the full $267m, plus whatever healthy profit is written into the plan as drafted by Aecon. That is a massive imbalance.

Again, this is not an objective statement. While overseas lenders and investors have to be repaid, the other side of the transaction is that a brand new airport terminal will be created that will be owned by the people of Bermuda. So there is no "massive imbalance," there is only the procurement of an infrastructure asset that is paid for over time.

40. On this major point of national economic stimulus, there has been no analysis - none whatsoever – by the Government of Bermuda or by Aecon. On this critically important economic stimulus matter, both are silent. However, the 'cost' of receiving forty months of economic stimulus must be set against 360 months of paying for that small and short burst of economic stimulus; and it is a proper matter for deep public concern.

    See the response to the previous point. Considerable information has been provided by the Government in the Entrustment Report, specifically on the Strategic Case for the project.

41. In dealing with the Airport [actually and specifically, the Air Terminal building] there are three alternatives:

    - One – do nothing. Just keep fixing up.
    - Two – Knock it down and build new.
    - Three – Repair, renovate, and re-build where and as necessary.

    The options identified represent the opinion of the Commentators with no objective support. The Government retained the services of an independent airport consultant which identified 9 options and the Government assessed the financial merits of each alternative. Consistent with the independent value for money report, the current option being pursued represents the highest value for money.

42. In order to determine the best way forward, the start point must be to seek an answer to this primary question: "What, exactly, does Bermuda need at the Airport?" This study will deliver two answers. Either demolish and rebuild. Or Repair and maintain. The next logical step is to determine cost and current or near future affordability. Such a process means starting from zero.

    The Government started at zero and considered all the evidence from highly experienced advisors, including the Airport Master Plan produced 10 years ago. The current state of infrastructure is on borrowed time. The Government could invest millions of capital into the terminal which would need to be replaced in the next several years or build a new terminal. The Government determined that it did not make any sense to invest in an aging terminal that would need to be replaced in the near future. This would only delay the inevitable, cost the Bermudian taxpayer more money and potentially result in a significant increase in the costs of the project as interest rates are at all-time lows. This decision was supported by the government's internal analysis as well as the independent SDG analysis.

43. The process currently underway did not start from zero. Instead, it started, in 2006, with the single and un-researched premise: "Bermuda needs a new Airport." That start was and remains wrong. Totally wrong.

This is a statement of opinion that is not supported by experts or the facts on the ground. First, this was a very well researched topic. Two, an internationally recognized engineering firm as well as the engineering head of the airport concluded that a new airport is needed due to the current state of the infrastructure and susceptibility to storm surge based on the current terminal footprint.

44. In 2016, Bermuda's extraordinarily high financial risk profile shows:

    - $20 out of every $100 spent by Government has been borrowed;
    - Government priority pays out $18 out of every $100 of revenue that it takes in, and pays that out to service its Debt
    - Government's Gross Debt [$2,484 million] is currently 250% greater than Governments hoped for 2016/17 revenue of $997m.
    - Government has [or will have] borrowed $1,665 million in the 35 months between December 2013 and November 2016
    - Daily Debt Service costs are budgeted at $513,356 a day; and scheduled to rise higher.

    All of this puts Government's near-term outlook in a precarious and high-risk state where the slightest drop-off in revenue could combine with a surrendering of revenue and cause Government to again go running back to the lender's market in mid-2017 for another big tranche of borrowed dollars.

The Government is fully cognizant of the fiscal situation and the importance of not over-burdening Bermudians with debt. As a result, the airport redevelopment project is being funded through the G2G model that transfers the debt/financial risk to the private partner and the performance risk to the Canadian government, thereby mitigating the possibility that the Government might incur more than the established affordability cap.

45. Continued borrowing at our current rate will quickly cause a downgrade by the Rating Agencies. This will see Bermuda's sovereign Credit Rating drop from Moody's A2 to Moody's Baa1 or lower. Once in Moody's B's, all borrowing costs will rise and Bermuda will require a huge and rapid expansion of its real economy, if Bermuda is to survive as we know it today.

This project was specifically pursued because it DID NOT result in significant sovereign borrowing or an increase Bermuda's sovereign debt. The debt will be raised by the separate special purpose vehicle that will have no recourse to the Government.

46. Hence, and specifically with regard to the Airport, the matter of 'affordability' should be the paramount consideration. The Aecon plan considers affordability, but only from Aecon's narrow profit-seeking perspective. A clinical analysis of true and real costs, shows that the Airport scheme as proposed by Aecon will cost far more than is indicated in their papers and documents; and that the real costs – to Bermuda and Bermudians – is far higher than is reflected in Aecon's voluminous documentation. *[See paragraphs 49 – 61]*

The analysis provided by the Commentators is anything but clinical – it is replete with errors. The most important element to the Government was affordability to the Bermudian people. Specifically, an airport that was affordable and delivered the highest value for money to the Bermudian people. To ensure that it came to a correct conclusion, the Government retained services of several internationally recognized firms to assist in its analysis of all potential options. The Government did not want to make significant errors and come to the incorrect conclusion.

The Government reviewed the poorly crafted analysis highlighted in paragraphs 49 -61. The analysis contained gross errors and was created in a way to materially mislead the Bermudian public. When one looks at the actual figures, it is clear that the project is affordable to Bermuda.

47. Essentially – when real costs are factored in - the Aecon P3 becomes far too costly an option, at this time.

The analysis prepared was easily disproven by the Government due to the widely inaccurate assumptions used. Please refer to paragraphs 49 to 61 for analysis.

48. That leaves the best option as a Repair, Renovate, and Rebuild where necessary as the only sensible alternative. This RRR can be over three to five years. It can be funded by the revenue streams that are currently being set up and directed to Aecon. At a basic $37m a year, this funding would range from a three-year RRR outlay of $110 million to a five-year outlay of $185 million. None of these funds would have to be borrowed. There would not be any contingent liabilities. Bermudian workers would get employment. GDP would get more or less the same small boost.

First, current 2016/17 airport net cash flow is approximately $18.2m ($37.2m revenues less $19.0m expenses) instead of $37m. Second, the current airport net cash flow includes the new Airport Improvement Fee introduced specifically for the project as communicated to the airlines. There is uncertainty as to the level of airport fees that the airlines would accept if the capital expenditures are significantly less than the current project as these fees would not be approved by IATA. Third, with only up to $18m available, only suboptimal band-aid fixes are affordable. Fourth, these figures do not include maintenance capital expenditures which are currently a minimum of $5 million per year and are expected to increase.

A DETAILED ANALYSIS OF THE CASH FLOWS AND TRUE COSTS

49. Bermuda Cash Flow Model. By improperly omitting the Revenues that the Government will transfer, annual financial contributions to Project Co are $45.3m instead of the $14.9m assumed, at present, by the Government.

The Government's analysis has not omitted the revenues that the Government will transfer. This is a misunderstanding by the Commentators. This misunderstanding appears to stem from the difference in the approach used by them and that used by the Government.

The financial analysis approach used by the Government is based on the comparison of the cost to the Government under the different options (i.e., proposed G2G transaction and the Public Sector Comparator). This approach is standard practice and is per the UK Green Book. The analysis has been prepared with the assistance of internationally recognized experts and independently reviewed by another internationally recognized firm.

Under the Government's approach (according to the Green Book and independently reviewed) the Public Sector Comparator properly considers the revenues that the Government would have generated under a no P3 scenario. It is therefore incorrect to suggest that Government's analysis has omitted revenues that Government would have earned.

The apparent "omission" identified by the Commentators only appears due to the way they choose to construct the analysis and it has no impact on the validity of the Government's analysis.

Under the Commentators' approach, a comparison is made between cash flow to the Government before and after the P3 transaction and the difference is considered as the "cost" of the transaction. There are a number of major problems related to this approach:

- **The analysis on its own is incomplete as no other option is put forward for comparison. Even if the "cost" under the P3 transaction is as calculated by the Commentators, there is no frame of reference since the equivalent "cost" of the alternative is unknown.**
- **The "cost" of the foregone airport net cash flow in 2016/17 ($27.0m as calculated by B&M) would have been applicable to any other option and would impact each option equally. Accordingly, the $27m figure is not relevant for comparing different options. The focus should be on comparing the <u>future</u> costs under each option. The inclusion of the "missing" $27m/year as cost is misleading as that cost is at best an opportunity cost. Cash flow analyses don't add opportunity costs to cash flows.**

50. The Government developed a model ("Bermuda Cash Flow Model") to capture all the direct and quantifiable financial contributions by the Government to the Project. The model served as verification of the annual contributions that the Government was responsible for during the Project term. The Government determined the Total Annual Financial Contribution to Project Co to be $14.9m as follows.

Annual Financial Contributions per the Government	$m
Retained Government Services	8.8
Energy Supplement	2.6

BAA costs (Quango)	3.5
Annual Contributions per Bermuda model	14.9
Foregone cash (per MPs Summary –	3.4
Total Future Costs per the Government	18.3

This is a misrepresentation of the Government's analysis. With the exception of the BAA costs of $3.5mn, none of the other retained services will be new expenses, as government is currently paying for all these things, including electricity, already. Just because they are contributions government will make to the project doesn't make them additional cash flows. It does not represent the annual cost to the Government over the future 30 years. The $3.4 million in foregone cash is the net operating cash flow from 2015/16 and should be excluded from the $18.3 million.

51. Total Airport Revenues (2016/17 Account Estimates) are forecast to be $37.2m. (Departure Taxes $19m plus Airport Operations $18m). As all airport revenues will be transferred to Project Co., Government's cash flows will be lowered by the amounts of Revenue transferred to Project Co.

    The Government notes the following errors with the analysis:

    1. **This is based on the 2016/2017 forecast and not actual figures. Previous analyzes have focused on 2015/2016 figures which are actual figures and not forecasts**
    2. **If one uses the $37.2 million revenues from the 2016/17 budget estimates, several adjustments need to be made to reflect the actual amounts of revenue to the Government under the status quo scenario:**
        a. ***Airport Infrastructure Charge (AIF):*** **The Airport Infrastructure Charge (AIF) of $16/passenger was only adopted to support the project. In the event that the project did not go through, Bermuda could no longer levy this fee. Specifically, under IATA guidelines, one can only introduce fees to pay for capital improvements or supporting existing airport operating costs. As a result, one cannot include this in the analysis as this fee would disappear under the status quo option where Bermuda retained the airport and did nothing. The revenue associated with the AIF is $6,150,000.**

    In summary, using the 2016/17 forecast, the forecasted revenue to the airport is $37.2 - $6.2 = $31.0 million

52. In addition to transferring $37.2m/year in revenues, Project Co will take over $10.2m/year in expenses previously incurred by Airport Operations. Accordingly, the Government's annual cash flows will be reduced by $27m as follows ($m):

Omitted Annual contributions	$m
Revenues transferred	37.2

Less Airport Expenses transferred	(10.2)
Omitted Revenue Transfer Contributions	27.0
Total Future Costs per the Government	18.3

Total Annual Financial Contributions by the Government 45.3

The Commentators' analysis misses several cash flows that need to be included. In particular, the analysis does not include the transfer of capital expenditures. In fact up-front cap-ex costs required to make urgent near term repairs to the existing terminal as well as some improvements to the facility that are necessary to continue operations were estimated by GOB's technical advisor to be $62.3 million in repairs and $104.8 million in improvements in a 2013 report. In addition ongoing maintenance costs need to be also included.

The Commentator's analysis also does not include the net savings to the Government of $1 million for central Government costs no longer paid for by the Government and transferred to Project Co.

It should be noted that the above excludes the potential for the Government's 50% sharing in the upside of the project. The broader economic and tax benefits of the project are also not included. Hence the Government's deficit increase as suggested by the Commentators is significantly overstated.

The analysis is flawed because it focuses on the opportunity cost of lost revenues rather than the net present value of all options available. Another flaw is that, as already stated, the Government's contributions of retained services and energy are not extra costs to government, as they are already being paid for. Moreover, it conveniently omits construction costs and financing costs which are significant. The standard market practice for assessing infrastructure projects globally and the approach the Government has used is also in line with the U.K. Green Book. The approach used by the Commentators is not an accepted method to look at projects as it mixes cash flows with opportunity costs, which by the way they computed incorrectly. Their conclusions are therefore misleading the public on the merits of the Project.

53. **The Government assessment of Affordability of Financial Contributions**. Based on the output from their model, Government determined the relative impact on the Government's overall fiscal balance and whether it was reasonable from an overall Government affordability perspective.

This report fails to mention that this was also supported by the independent third party who determined that the approach being pursued leads to the highest value for money. This firm is highly experienced is preparing value for money reports on an international scale.

54. Government concluded: "*When compared to the Government's Consolidated Fiscal Balance for 2015/2016, the impact of the financial contributions was found to be approximately 0.6% of this Consolidated Fiscal Balance. As a result of this analysis, the Ministry of Finance concluded that the Project-related financial contributions were acceptable from a Government fiscal position perspective.*"

This is correct. When using legitimate figures the impact is 0.6%. Specifically, taking the $14.9 million per year divided by the consolidated deficit of approximately $2.2 billion, the impact is 0.6%

55. Due to the Government's understatement of costs ($27m/year or $810m over 30 years) its calculation of Financial Contribution costs to Consolidated Fiscal Balance (0.6%) was a third of the actual amount (1.8%). <u>This error invalidates Governments calculations and analysis.</u>

The errors made by the authors of this paper invalidates all of their respective calculations and analyzes. Effectively, they have attempted to mislead the public and fabricate numbers that support their pre-determined opinion which is not supported by any independent analysis.

56. By omitting the cost of Net Revenue contributed to Project Co ($27m) the Government has understated the cost of the Airport by $810m (30 x $27.1m/year) **<u>As explained, the Government has omitted cash costs of $810m in respect of Net Revenues contributed to Project Co. Consequently, the actual Airport Cost ($1.4bn) is nearly 2.5 times the Government's cost of $549m as follows ($m):</u>**

	Annual	x30	Total
Future Annual Cost per the Government	18.3		549
Cost of Net Revenues transferred to Project Co	27.0		810
True Cost including Net Revenues Transferred	45.3		1,359

As stated above, the analysis is materially flawed and uses widely incorrect figures. Also, showing undiscounted figures over a 30-year term significantly overestimates the net impact to Bermuda. The only way to look at this is using a discounted cash flow analysis and not on a nominal basis. If you were to look at this on a nominal basis, the analysis would need to be amended to use the correct figures:

	Annual	x30	Total
True Cost including Net Revenues Transferred (Previous)	45.3		1,359
True Cost including Net Revenues Transferred (Actual)	24		720

An analysis which overestimates costs by approximately $600 million is not something that can be relied upon.

However, the Government notes that this is a flawed analysis as this is looking at the opportunity cost of lost revenues rather than the net present value of all options available. The latter is standard market practice for assessing infrastructure projects globally and the approach the Government has used which is in line with the U.K. Green Book. The approach used by the Commentators is not an accepted method to look at projects and is an attempt to mislead the public of the merits of the Project.

57. **Implications** <u>This error invalidates all of Government's analyses and conclusions involving Airport cost. The enormity of this error invalidates Government analyses and conclusions in most financial areas including but not limited to:</u>

(i) Net Present Value calculations in the Financial Comparisons Report;

(ii) Value for Money Calculations made by Government

(iii) Steer Davies Gleave Value for Money Report

(iv) Project Options Analysis in Overall Business Case

(v) Cash Flow Summary Appendix 9 (Overall Business Case)

(vi) Calculations of Cash Flows for all DBFOM analysis

(vii) Credit Rating Impact of Project Cash Flows

(viii) Economics of Revenue Guarantee and its potential impact on Government Debt

(ix) All analysis and projections of Government cash Flows and Debt Impact

The treatment of foregone net revenues as costs is not standard practice. The approach used by the Government is according to standard practice and has been reviewed by an independent expert.

58. The substantial magnitude of the $810m cost omission renders all supporting financial analysis invalid. Government's financial analysis has little if any credibility. A project now shown to be costing $1.4bn is clearly not justified. All debt metrics and affordability analysis are invalidated.

Simply put, the analysis put forward by the authors of this paper did not meet the bar of being credible due to the level of errors made. The Government retained third party advisors for this very reason to avoid making such errors and coming to the incorrect conclusion.

<u>Financial Analysis Section Summary</u>

59. Bermuda is amidst a Fiscal Crisis driven by excessive Debt. During the last 6 years, the Government Expenses have exceeded Revenues by 35%. Debt has grown sevenfold from $335m to $2.4 bn. Net Debt is currently three times the sustainable level (Net Debt Target), and is more than twice Revenue.

This project was specifically pursued because it did not result in significant sovereign borrowing or an increase Bermuda's sovereign debt. The debt will be raised by the separate special purpose vehicle, Project Co. Project Co's lenders will have no recourse to the Government of Bermuda.

60. If this project were implemented (cash cost of $45m/year) and the Government could maintain steady Revenue growth at 3% and steady Expense control at 0%, it would take 12 years to produce a surplus and 24 years to reduce Net Debt to the sustainable Net Debt Target. This could spell disaster for the Government's credit ratings and ability to finance future longer term operations.

Please refer to analysis above.

61. Note that 12 and 24 years encompass three and six General Election periods with the possibility of as many as three and six different political parties or political administrations managing Bermuda's national finances.

The term of the concession is consistent with benchmarks from around the globe. The independent VFM report confirms this. It is universally accepted that investing in a country's infrastructure over the long-term is paramount to economic growth.

CONCLUSION

62. **Considering all of the facts and factors set out in these 11 pages, this project, with its real thirty-year costs to Bermuda of $1.4bn, must be put on hold pending an entire review and full explanation of its true financial and qualitative factors.**

Overall, it is evident through the numerous errors and incorrect assumptions made by the Commentators that they lack the knowledge and experience in several areas and their conclusions are not credible. The Government retained several third party advisors with global experience such that these types of errors would not be made and that the correct conclusions would be reached.

The public is encouraged to read the Overall Business Case report in its entirety. However, recognizing the comprehensive and technical nature of the content, the summary report is intended to provide an overview of the key aspects of the Project.

Of particular note is the Value for Money ("VFM") assessment undertaken by independent consultant, Steer Davies Gleave ("SDG"). The VFM assessment highlights how the Airport Redevelopment Project compares with similar P3 deals and concludes that overall the Project achieves value for money for the people of Bermuda.

-END-