

Date : 10/7/2010 2:01:33 PM

From : "Hammond, Vaughn"

To : "Harvey, Michael"

Subject : FW: LC Federal guarantee process note 6 (2).doc

Attachment : LC Federal guarantee process note 6 (2).doc;

Michael,

Bob simply inserted the information that we sent him yesterday. I don't have any substantive concerns with the note.

Vaughn

From: Constantine, Robert

Sent: Thursday, October 07, 2010 1:50 PM

To: Hammond, Vaughn; Harvey, Michael

Subject: LC Federal guarantee process note 6 (2).doc

The draft is now at a place where I can share. I will need any comments very quickly, as Terry wants to give it to the Minister this afternoon.

**Department of Finance
Briefing Note**

Issue: Request for a Federal loan guarantee for the Lower Churchill project

Background

Process

- There is no formal loan guarantee program available to public authorities within the federal government. Any request for financing assistance through a loan guarantee by a public authority would be ad hoc.
- In the absence of a formal program with established criteria, the consideration of alternative approaches to the federal government should evaluate the likelihood of a receptive outcome.
- Historically, ad hoc requests to the federal government at the officials level have not been successful. Generally, some level of commitment at the political level may be necessary in order to advance any proposal.
- The magnitude of this project and any potential assistance would suggest that a commitment at the First Minister level would be the most appropriate approach. While other possible approaches include a letter from the NL Finance Minister to the federal Finance Minister or a letter from the NL Deputy to the federal Deputy, it is unlikely this would achieve the desired results.
- It is likely that considerable information around the project from both a technical and economic/financial perspective will be necessary, should there be receptivity. NL will have to provide sufficient information for the Government of Canada to evaluate the project. This will necessarily entail releasing commercially sensitive information. A balance is required between providing sufficient information to inform the request while limiting the disclosure of commercially sensitive information to what is essential. This would likely occur at the officials level but may also include elected officials as well.
- The scope of a request for a loan guarantee may affect the current approach to project financing. Items which may affect the approach could include the following:
 - Consideration of the project components which could be the subject of the guarantee;
 - Whether the borrowing to fund the project will be done directly by Nalcor, or a subsidiary, or whether the Province would borrow and inject the funds as equity
 - The proportion of project costs that would be financed;
 - The specific terms of the guarantee i.e., guarantee the debt, or guarantee construction only, and the method or timing of an exit strategy for the guarantor;
 - The guarantee fees or benefit to the guarantor that might apply, if any; and
 - The possible support that might be available from other Provinces, if any.

- Any approach to the federal government could point out that the request is not related to inherent risk of the project. The size of the Lower Churchill Project and capital requirements are very significant in relation to the fiscal capacity of the Province. Provincial borrowings or loan guarantees could impede the flexibility to borrow for other government activities.

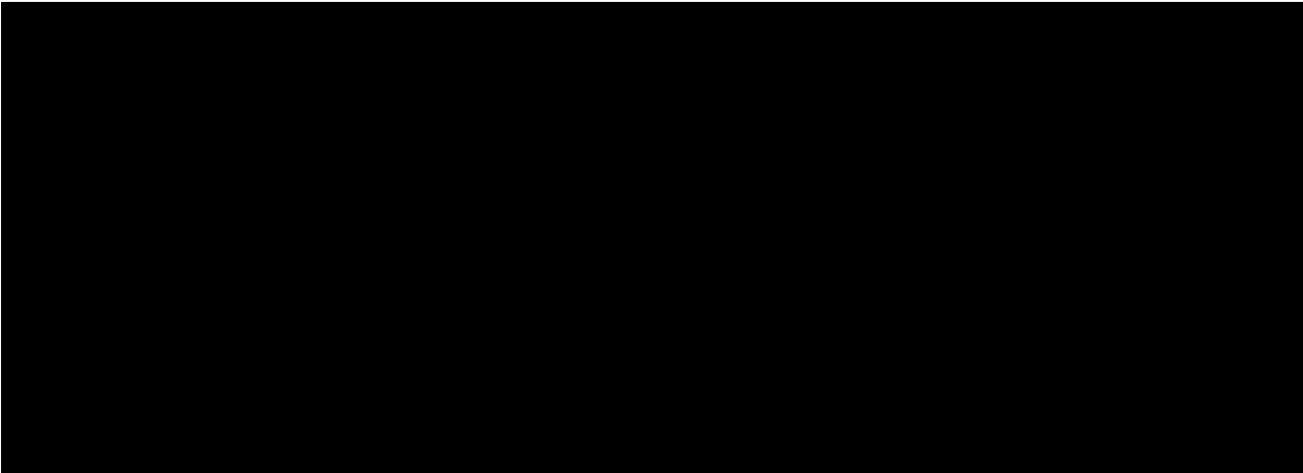
2005 Election Commitment

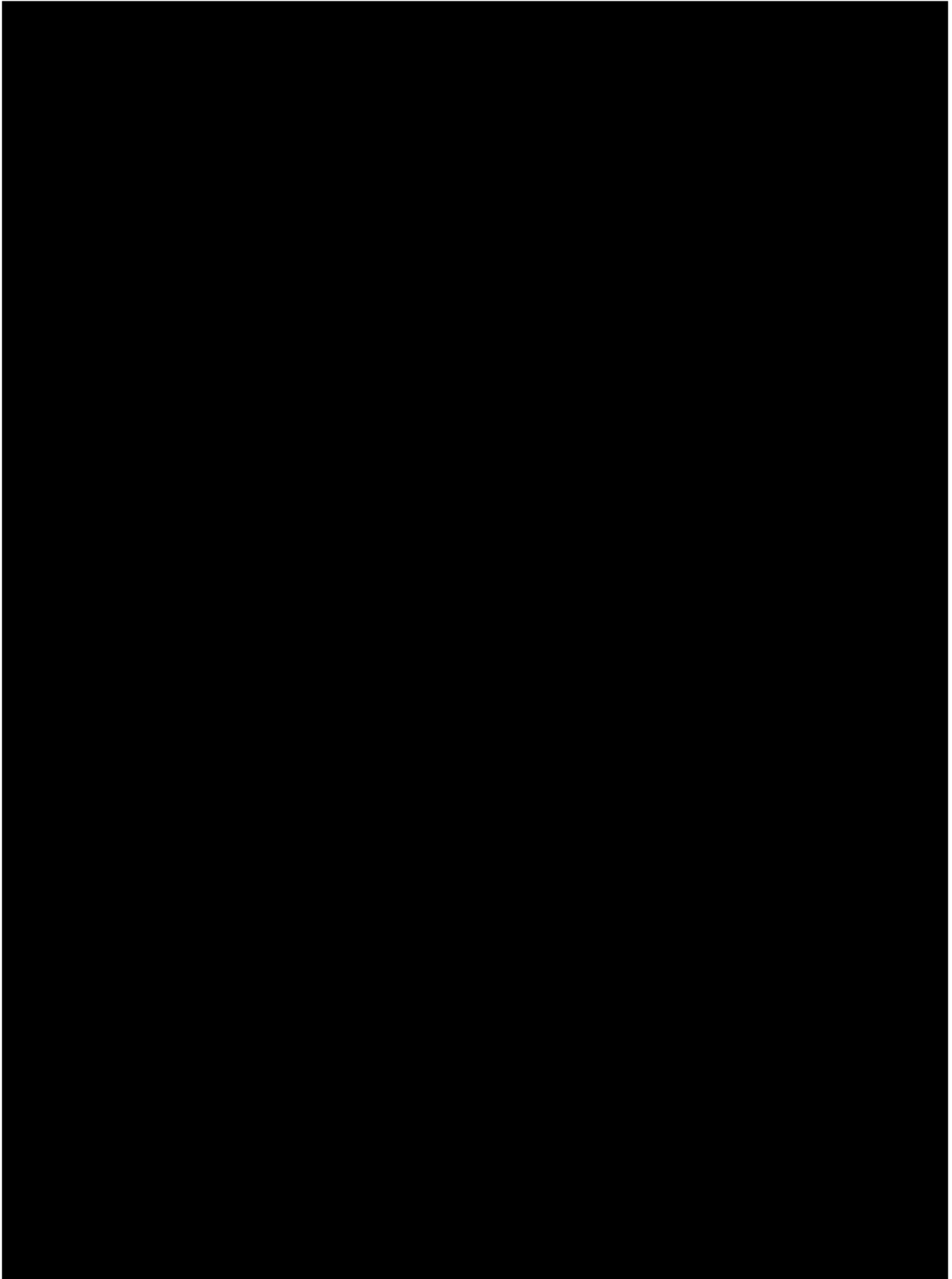
- The following is a transcript of an interview on December 5, 2005, with then Opposition Leader Stephen Harper with Debbie Cooper of CBC:

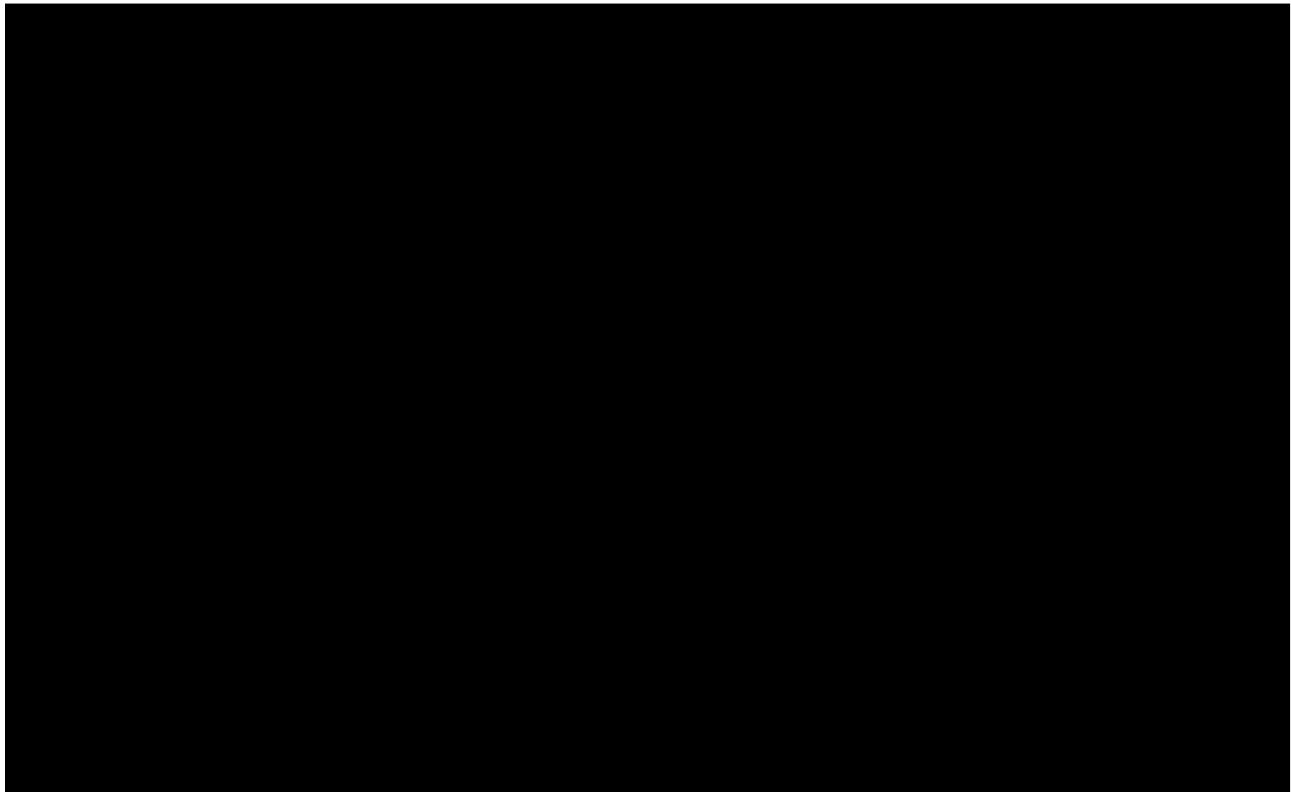
“DEBBIE COOPER: The Prime Minister also is committed, he says, to helping the province develop the Lower Churchill project. Kind of scanty on details, it is early. What would you do?

STEPHEN HARPER: Well, I’ve talked to Premier Williams a number of times on this. I’ve always been clear. I think he’s looking for the federal government to play some kind of role in the way of a loan guarantee. I’ve said we’re certainly prepared to do that. We obviously have only had preliminary discussions on how that would be structured, but the truth is there has been legislation in place both federally and provincially for over 30 years now setting up a joint corporation, allowing for the federal government to get involved in this, and I think we owe it to Newfoundland and Labrador because of what happened with the Upper Churchill to help. We have a market in Ontario which is going to need the power. So I think it’s something we can get on with.”

Timing of Request

- Any indication by the province that it is committed to the project prior to a request to the federal government will likely weaken its argument that the guarantee is necessary to mitigate impacts on the provincial borrowing capacity.
 - The province may wish to secure some commitment from the federal government to review its request for a guarantee prior to any communication surrounding project scope.
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Benefits to the Project

- Nalcor estimates the project benefits of a federal guarantee, as follows.

PROJECT COMPONENT	TOTAL IN-SERVICE CAPEX (billions)	TOTAL DEBT (billions)	NET BENEFIT (millions)
Maritime Link	Lo - \$1.4; Hi \$1.5	Lo - \$0.9; Hi \$1.1	Lo - \$90; Hi \$160
Muskrat Falls	Lo - \$3.4; Hi \$3.6	Lo - \$1.8; Hi \$2.9	Lo - \$230; Hi \$390
Island Link	Lo - \$2.6; Hi \$2.6	Lo - \$1.9; Hi \$2.0	Lo \$190; Hi \$290
Gull Island	\$8.2	\$6.5	Lo \$460; Hi \$730
Total Potential Benefit	Lo - \$15.6; Hi \$15.9	Lo - \$11.1; Hi \$12.5	Lo \$970; Hi \$1,570

- These benefits would be reduced by a guarantee fee, if any.

Benefits to Canada

- A letter requesting a guarantee for the Lower Churchill Project should articulate why federal support is in the national interest, and should provide some detail upon the benefits to Canada.

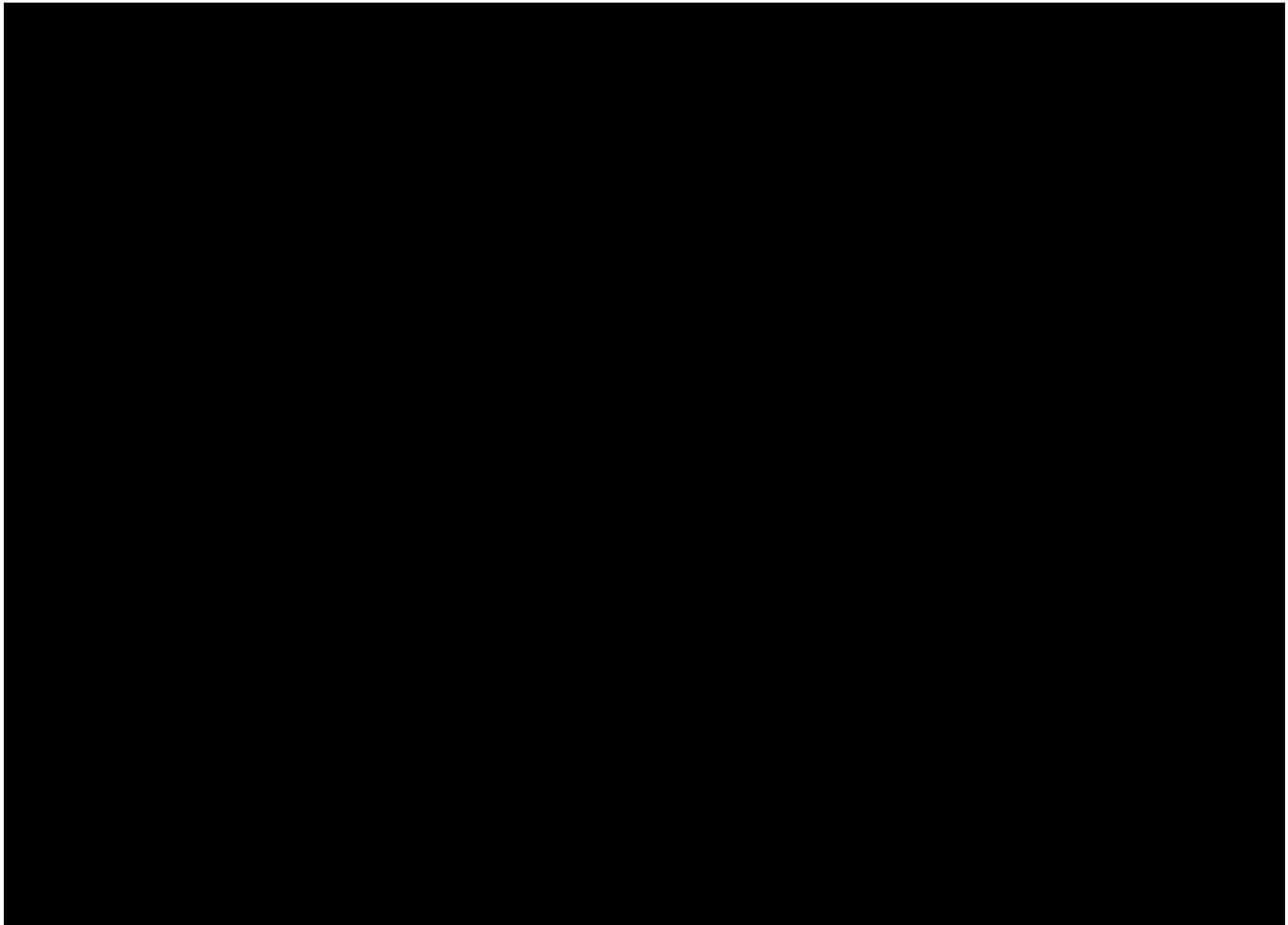
- The benefits to Canada would be economic benefits, such as direct, indirect and induced employment, as well as labour income. There would be positive treasury impacts for Canada, NL and other provinces. Environmental benefits include reducing the carbon emissions, contributing to Canada's 2020 emission reduction targets and having tradable carbon credits. The Lower Churchill Project could also contribute to Canada's Energy Security and reduced reliance on fossil imported fuels.

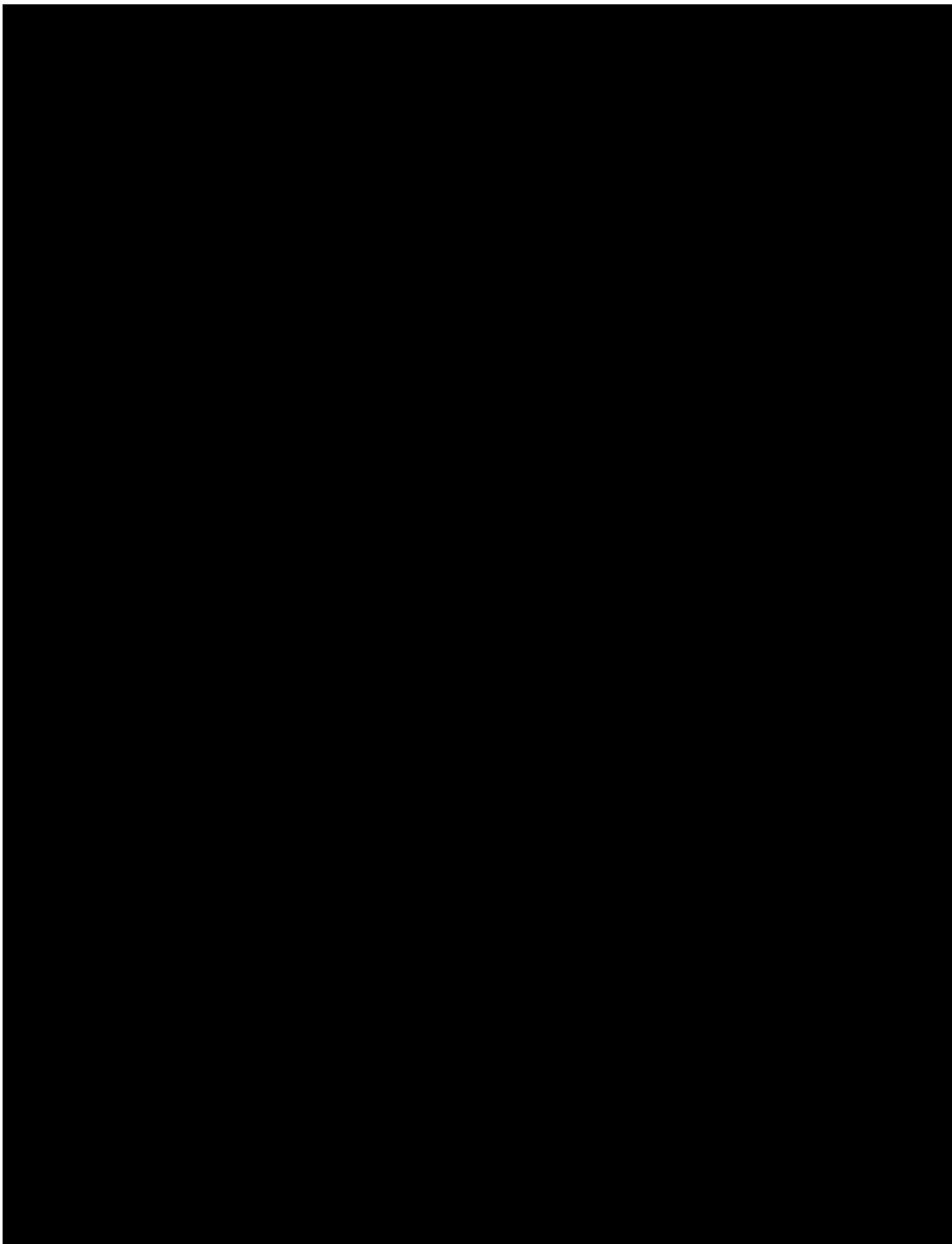
Economic Benefits

- Nalcor has completed an economic impact analysis (January, 2009) on the Gull Island Project with island link and Maritime link, but has not yet completed an economic impact analysis on the Muskrat Falls Project. The economic impacts should be articulated in the letter requesting the guarantee, and should be consistent with the project specified in the scope of the ask.

Precedents

- The case for the federal government providing a guarantee for the project would be more compelling if it could be bolstered with specific references to similar support for other projects. Research to date is outlined below.







Support from Other Provinces

- A request for federal support for the Lower Churchill may gain more traction if supported by other provinces.
- The Province of Nova Scotia is aware of confidential negotiations between Nalcor and Emera with respect to the construction of the Maritime Link. Any reductions in cost associated with the construction of the Maritime Link would help alleviate costs to ratepayers in Nova Scotia. Consequently, the loan guarantee would likely be viewed positively by the Province of Nova Scotia.
- In addition, the Department of Energy of the Province of Nova Scotia was a cosignatory to the P3 submission for the "Atlantic Provinces Renewable Energy Interconnect" (Maritime Link). It is reasonable to suggest that this action denotes support for the Lower Churchill project and hence, a degree of implicit support by Nova Scotia for any financial assistance by the Federal Government that would facilitate construction of the project.
- Nalcor advises that with respect to New Brunswick, Prince Edward Island, Quebec and Ontario, the presence of the Maritime Link could provide them with another source of clean energy at reasonable cost. To the extent that the Federal Loan Guarantee facilitates completion of the Project, it is logical to think that all these provinces might view such an application as being in their own interests and perhaps support it.

Consultations

- This note was prepared by the Department of Finance with the support of, and input from, the Department of Natural Resources, Nalcor and the Intergovernmental Affairs Secretariat.

Prepared by: Bob Constantine

Approved by: Terry Paddon

Ministerial Approval:

Date: October 7, 2010