Re: Item No. 13.2.1

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Irving Shipyards Agreement

Background

- In 2012, Irving approached the city with several issues related to the impact of National Shipbuilding Procurement Strategy contracts.
- One of the issues was the assessment of the Barrington property, and later the Burnside property, given the difficulty assigning a market value to special purpose industrial property in general, and their site in particular.
- Staff worked with staff from ISI, and property appraisal experts from then until March 2014, when Irving wrote to the CAO seeking an agreement and proposing a methodology.
- Council agreed in principal in April 2014, and directed staff to negotiate an agreement in keeping with the method proposed, and to approach the Province for enabling legislation.

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Legislation

- Bill 59 was passed by the Provincial Legislature in the Fall 2014 session to enable tax agreements for “eligible industrial properties”.
- It also required that agreements be approved by by-law.
- The Ministerial regulation (11/2015) defining “eligible industrial property” was filed with the Registrar of Regulations January 26, 2015.
- This enabled the municipality to proceed.

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Reason for an Agreement - 1

- The tax agreement is a high priority for ISI for two reasons.
- First, the Canadian Government benchmarks their shipbuilding costs by having a third party evaluate their proposals to design and build the Arctic Offshore Patrol Ships (AOPS) and Canadian Surface Combatant (CSC) vessels, and ISI must provide full transparency on costs. These costs must be competitive as early as possible in both the AOSP and CSC projects as ISI will be required to commit to firm fixed prices.
- Second, ISI will be bidding on the In-Service Support (maintenance) contract for AOPS in 2015. This $2 to $4 billion dollar contract will be critical to sustaining the shipyard. Since this work will be competitively bid, competitive input and overhead costs such as property tax will be a key factor in successfully winning the bid.

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Reason for an Agreement - 2

- Rather than proceed through the assessment and appeal process, followed by likely court action, both parties felt it is in their mutual interest to reach an agreement, and thus provide certainty to the costs for Irving, and the tax revenue for Halifax.
- Assigning a market value to industrial properties is difficult due to their unique nature and lack of sales of comparable properties. Assessors usually rely on cost as a proxy.
- In addition, the yard is overbuilt for any purpose but fulfilling the CSC portion of the contract, and therefore the market value, should it be sold to another party for other work, would be significantly less than the cost to construct it.
- The agreement recognizes the significant economic obsolesce associated with the properties.

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The Agreement

- At no point will Irving Shipbuilding Inc. (ISI) pay less tax than they currently pay, in fact this base amount will increase by 1% per year, more if inflation reaches 10%
- Irving will pay additional tax based on future employment levels at the yard. Using projections for the work required for the two contracts – the Arctic Offshore Patrol Ships (AOPS) and Canadian Surface Combatant (CSC) vessels – this agreement will generate an additional $22 million tax dollars for Halifax, almost $1 million dollars per year.
- The tax will vary from year to year depending on employment levels, starting at the current annual level of $576,476, increase to peak of $2,346,661 and decline to $1,888,836 in the final year of the agreement. That is $1.3 million more than the current tax bill.

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Risk Management

- The agreement bases the tax on employment levels at the facility. The main risk to manage is that ISI sources work elsewhere, reducing the workforce at the two sites.
- ISI is heavily motivated to use the sites because:
  - ISI invested $350 million creating a modern, efficient facility
  - Of the $350 million, $260 million was financed with a loan from the Province. The loan is forgivable based on jobs at the sites.
  - The Collective agreement at the sites has language covering contracting out, and Agreement will count these positions if this happens
  - ISI invested heavily in training the current work force, including partnerships with NSCC.

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In Closing

- This agreement is not about reducing Irving's tax bill, but determining how much additional tax they will pay.
- Agreements like this, using a proxy like employment levels to determine value, are not unique. The agreement for the Imperial Oil refinery was based on the throughput of barrels of oil. The agreement with the Halifax International Airport Authority is based on passenger volumes.
- Halifax is fortunate to have this significant industry, and recognizes the significance of the approach the Federal Government used for the National Shipbuilding Procurement Strategy, an approach designed to promote a sustainable industry.

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