Value for money review

Independent Review of the NRA Agreement between Dart Realty (Cayman) Ltd, the NRA and the Cayman Islands Government

May 2013

pwc

DRAFT – For Discussion Purposes Only

Basis of Preparation and Disclaimer

Basis of Preparation

This draft report has been prepared solely for the purpose of providing the Cayman Islands Government ("CIG" or "Government") with our findings from the Value for Money Review ("Independent Review"), as required under the contract for VfM consultancy services dated 22 March, 2012, between PwC Corporate Finance & Recovery (Cayman) Limited ("PwC") and the CIG. PwC Corporate Finance & Recovery (Cayman) Limited is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.

Disclaimer

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In preparing this report PwC must stress that it has relied upon information provided by, amongst others, the CIG, the National Roads Authority ("NRA"), the Department of Lands & Survey ("DLS"), the Department of Tourism, the Economic Statistics Office, JEC Property Consultants Ltd, third party valuation experts, and DRCL. **PwC has not performed an audit examination on this information. Except where specifically stated, PwC has not sought to establish the reliability of the sources of information presented to them by reference to independent evidence. The financial analyses presented in this report are based on estimates and assumptions, and projections of uncertain future events. Accordingly, actual results will vary from the information provided in this report, even if some or all of the assumptions materialize such variances may be significant as a result of unknown variables.**

Hon. Premier Juliana O'Connor-Connolly, JP, MLA
Ministry of District Administration, Works, Lands & Agriculture
4th Floor, Gov't Admin Bldg,
71A Elgin Avenue,
George Town,
Grand Cayman

8 May, 2013

Dear Premier,

Independent Review of the National Roads Authority Agreement

We are pleased to present our draft report on the National Roads Authority Agreement, as required under the contract for VfM consultancy services dated 22 March, 2012, between PwC Corporate Finance & Recovery (Cayman) Limited ("PwC") and the Cayman Islands Government ("CIG").

In preparing this report, PwC has relied upon information provided by, amongst others, the CIG, the National Roads Authority, the Department of Lands & Survey, the Department of Tourism, the Economic Statistics Office, third party valuation experts, JEC Property Consultants Ltd and Dart Realty (Cayman) Limited. PwC has not performed an audit examination on this information. Except where specifically stated, PwC not sought to establish the reliability of the sources of information presented to them by reference to independent evidence. The financial analyses presented in this report are based on estimates and assumptions, and projections of uncertain future events. Accordingly, actual results will vary from the estimates provided in this report, and even if some or all of the assumptions materialize such variances may be significant as a result of unknown variables.

We would be pleased to meet with you at your convenience, to discuss the draft report and seek CIG's feedback on matters of factual accuracy. Following this, we will issue a final report, taking into account any additional relevant matters brought to our attention.

We appreciate the opportunity to assist you with this matter.

Very truly yours,

PwC Corporate Finance & Recovery (Cayman) Limited

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Glossary of Terms and Abbreviations

Term	Definition
ACR	The proposed Airport Connector Road, as defined in the NRA Agreement
ADR	Average Daily Rate, measure of hotel revenues by room
BOBR	Bank of Butterfield Roundabout on the ETH
Borrowing Limit	The Cayman Islands' public sector debt restrictions, as defined under the FFR and its transitional provisions
CIG / Government	The Cayman Islands Government
CTC	CIG's Central Tenders Committee
DLS	CIG's Department of Lands & Survey
DRCL	Dart Realty (Cayman) Limited, including its affiliates and successors
DRCL Development Plan	DRCL's preliminary estimates for real estate and tourism development alongside the WBR and ETH Extension over a period of over 25 years
ETH	Esterley Tibbets Highway
ETH Expansion	The proposed transformation of the Esterley Tibbets Highway from a two lane road to a four lane arterial road, from the Bank of Butterfield Roundabout to the Limestone Roundabout
ETH Extension	The extension of the Esterley Tibbets Highway from Raleigh Quay to Batanabo Road, as set out in the NRA Agreement
FCIA	The For Cayman Investment Alliance, representing a proposed partnership to be entered into by CIG and DRCL
FCO	The UK Government’s Foreign and Commonwealth Office
FFR	The Framework for Fiscal Responsibility agreed between the CIG and FCO on 23 November, 2011
First Amendment	The amendment made to the NRA Agreement dated 28 April, 2012
FSIM	Financial services indirectly measured, an estimate of the impact financial flows in an economy
FTE	Full-Time equivalents, measure of employees
GVA	Gross value added, a measure of economic benefits

Glossary of Terms and Abbreviations (continued)

Term	Definition
Hotel Tax Rebate	The NRA Agreement provisions for a 50% rebate to DRCL of all taxes levied pursuant to the Tourist Accommodations (Taxation) Law, subject to certain conditions
IFRIC 12	International Financial Reporting Interpretations Committee, Interpretation 12
IFRS	International Financial Reporting Standards
Independent Review, or the Assignment	The independent review of the NRA Agreement by PwC, commissioned by CIG and commenced on 22 March, 2012
IO Tables	Input / Output tables, economic analysis tools for the purpose of deriving multiplier impacts
IPSAS	International Public Sector Accounting Standards
JEC	JEC Property Consultants Ltd
LOS	Level of service, in the context of delays in road traffic flow
LSR	Limestone Roundabout on the ETH 2013
LTBR1	Lawrence Boulevard Roundabout on the ETH
New Public Beach	Public beach to be created in Barkers from land provided by DRCL from parcel 8A19 and a portion of parcel 8A20
NPV	Net Present Value
NRA	The National Roads Authority of the Cayman Islands
NRA Agreement	The agreement between CIG, NRA and DRCL, dated 15 December, 2011, and reflecting the First Amendment, the Second Amendment and the Third Amendment, which represents the subject of the Independent Review
PMFL	Public Management and Finance Law (Revised)
Public Beach Park	Park to be created on the Soto Land behind the existing public beach
PwC	PwC Corporate Finance & Recovery (Cayman) Limited. PwC Corporate Finance & Recovery (Cayman) Limited is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity

Glossary of Terms and Abbreviations (continued)

Term	Definition
REVPAR Report	Lodging Market Review Grand Cayman, prepared by REVPAR International for DRCL, 21 December , 2011
ROW	Right of way
Road Infrastructure	The road construction set out at Schedule 1 of the Terms of Reference, and referred to as 'infrastructure benefits'
Roads Law	The Roads Law (2005 Revision)
RSF	Rent per square foot
SAMs	Social Accounting Matrices, economic analysis tools for the purpose of deriving multiplier impacts
Second Amendment	The amendment made to the NRA Agreement dated 25 July, 2012
SMB Hotel	The land and buildings on Parcels 82, 83 and 84 of Block 11B of Grand Cayman (parcel 83 of which being the former Courtyard Marriott)
Soto Land	Parcels 11B7, 11B23 and 11B26, the leasehold of which is to be transferred from DRCL to CIG, which owns the freehold
Taxation Incentives	Generally, incentives offered to DRCL in the form of abatements or waivers of any form of Cayman Islands import and stamp duties, development fees, hotel taxes and other taxation
Terms of Reference	Terms of Reference for the Independent Review of the National Roads Authority Agreement, issued in final form by CIG on 24 January, 2012
Third Amendment	The amendment made to the NRA Agreement dated XXXX, 2013 [the version sent by DRCL to CIG on 12 April, 2013 has been used for the purpose of preparing this draft report]
Traditional Delivery Model	Construction and maintenance of Cayman Islands roads infrastructure by the NRA, under the remit of the NRA Law (2004) and the Roads Law (2005)

Glossary of Terms and Abbreviations (continued)

Term	Definition
UK GAAP	UK Generally Accepted Accounting Principles
VfM	Value-for-Money
WB Hotels	Four proposed hotel developments comprised in the DRCL Development Plan
WBR	Public road on Grand Cayman, known as West Bay Road, running along the peninsula from George Town to West Bay
$53m Abatements	DRCL's stamp duty, development fee import duty and SMB Hotel Tax Rebate up to an NPV amount of $53m, under the NRA Agreement

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1. PwC's assignment

1.1. Introduction

On December 15, 2011, the Government of the Cayman Islands ("CIG" or "Government"), the National Roads Authority of the Cayman Islands ("NRA") and Dart Realty (Cayman) Ltd. ("DRCL") entered into an agreement to promote tourism and real estate development by DRCL in the Cayman Islands, most notably by closing a portion of the West Bay Road ("WBR") and extending the Esterley Tibbetts Highway ("ETH") on Grand Cayman (the "NRA Agreement"). The NRA Agreement was subsequently amended three times:

- On 28 April, 2012 ("First Amendment");
- On 25 July, 2012 ("Second Amendment"); and
- On 12 April, 2013 ("Third Amendment"). **[To update should a new version be issued]**

For the purpose of this report, "NRA Agreement" refers to the original agreement signed on December 15, 2011 and the First Amendment, the Second Amendment and the Third Amendment, inclusively. **The Third Amendment remains unsigned and in draft. This report has been prepared on the basis that the Third amendment is signed in the form received by PwC on 12 April, 2013.**

The NRA Agreement includes an independent review process to be conducted by a qualified entity (the "Independent Review"). The purposes of the Independent Review are:

- To consider Government's compliance with the Framework for Fiscal Responsibility ("FFR"); and
- To provide Government with adequate information to assess the value of the NRA Agreement to the CIG and wider impact on Cayman Islands' economy.

CIG hired PwC Corporate Finance & Recovery (Cayman) Limited ("PwC") on 22 March, 2012 to carry out the Independent Review. To assist it in completing the Independent Review, PwC engaged as subcontractors, industry experts from PricewaterhouseCoopers LLP in Canada and PricewaterhouseCoopers LLP in the United Kingdom as well as with JEC Property Consultants Ltd ("JEC"), a Cayman Islands firm of Chartered Surveyors. PwC is solely responsible for the Independent Review. PwC Corporate Finance & Recovery (Cayman) Limited is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.

PwC issued a version of this report to CIG in May 2012, covering both the original NRA Agreement and the First Amendment. Following the issuance of that report, CIG and DRCL negotiated a number of changes to the NRA Agreement, leading to the signing of the Second Amendment in July 2012. PwC subsequently issued a revised draft version of this report in October 2012 to reflect changes made by the Second Amendment. Following further negotiations, CIG and DRCL issued a Third Amendment on 12 April 8, 2013. **[To update should a new version be issued]** This report was prepared by PwC to reflect the changes made to the NRA Agreement by the Third Amendment. This report therefore entirely replaces our report dated October 2012.

1.2. Terms of reference

The terms of reference for the Independent Review as prepared by CIG are provided in Appendix A (the "Terms of Reference"). They set out the scope of the Independent Review, which consists of five components:

1. A value for money ("VfM") assessment of the NRA Agreement, comparing the value of the benefits received by CIG to the value of concessions made by CIG to DRCL;
2. An assessment of the NRA Agreement's contribution to the economic, social and infrastructure needs of the Cayman Islands;
3. An assessment of the NRA Agreement's compliance with the FFR;

4. An assessment of the risks for CIG relating to the NRA Agreement; and
5. The identification of realistic alternatives for CIG to finance the construction of the road infrastructure foreseen in the NRA Agreement.

The NRA Agreement was developed as a component of a broader agreement between CIG and DRCL called the ForCayman Investment Alliance ("FCIA"). PwC understands that as at the time of preparing this report, the FCIA has not been finalized. PwC has not been provided with a draft or final version of the FCIA agreement and it has been agreed with CIG that the potential terms and any possible impact of the FCIA are outside the scope of this Independent Review.

1.3. PwC's Value for Money methodology

The main purpose of the Independent Review, as set out in the Terms of Reference, is to assess whether the NRA Agreement provides CIG with value for money. The term VfM is widely used, particularly in the analysis of project procurement or development alternatives, but there is no single commonly accepted definition.

According to the UK HM Treasury, "VfM is defined as the optimum combination of whole-of-life costs and quality (or fitness for purpose) of the good or service to meet the user's requirement. VfM is not the choice of goods and services based on the lowest cost bid. (...) VfM is a relative concept which requires comparison of the potential or actual outcomes of alternative ... options".[1] The UK HM Treasury proposes the use of this definition primarily in the context of comparative analysis of alternative policy options.

According to the National Audit Office in the United Kingdom, VfM is "making optimal use of resources to achieve their stated aims"[2]. Optimal use is further defined by the National Audit Office as "the most desirable possible, given expressed or implied restrictions or constraints.[3]"

In the case of the NRA Agreement, CIG is providing DRCL with land and future tax rebates in return for receiving from DRCL cash, land, public infrastructure and the commitment to undertake tourism-related real estate development (with the associated economic impact of such development). In essence this represents a barter transaction or, alternatively, a form of joint venture with the private sector. Accordingly, for the purpose of the Independent Review, PwC has assessed VfM by considering whether the value of the benefits which CIG expects to receive, net of costs to CIG, taking account of any value forgone by CIG , represents optimal use of public sector resources, given existing restrictions and constraints. Since the main purpose of the Independent Review is to assess the NRA Agreement's value to the Cayman Islands, benefits provided by CIG to DRCL are analyzed from the perspective of their cost to (or value forgone by) CIG and not in terms of their potential value to DRCL.

The impacts of the NRA Agreement can be broadly divided into three different types:

1. Financial;
2. Economic and social; and
3. Risk-related.

The financial impacts represent the costs and benefits to CIG viewed from the perspective of the public finances in the Cayman Islands. They include cash, transfer of real estate, construction of infrastructure, increase in the value of real estate and financial compensation which would normally be paid, as well as rebates and waivers of taxes and fees otherwise charged by CIG.

The economic and social impacts are the net impacts which are estimated to accrue to the Cayman economy and to its citizens as a result of the NRA Agreement. The principal impacts are those on the tourism sector (which provides the prospect of faster economic growth and improved employment prospects), on the road

[1] HM Treasury, 2006, Value for Money Assessment Guidance, page 7
[2] National Audit Office, 2011 Annual Report, page 13
[3] National Audit Office, 2011 Analytical framework for assessing Value for Money, page 1

network (potentially reduced travel time and increased safety) and investments of the grant provided by DRCL in CIG housing and other social programs.

Quantifiable risk-related impacts relate to risks which CIG would otherwise take responsibility for in absence of the NRA Agreement and which would represent a potential cost. Such risks most notably include the risk of higher than expected road construction costs. Risks also include the potential for unexpected outcomes resulting from the NRA Agreement which could be to the detriment of the CIG, and the Cayman Islands generally. Non-quantifiable risks correspond to events such as a wider impact on competition as a result of incentives provided to DRCL, or timing and feasibility of the execution of the development plan by DRCL.

Each of these impacts is analyzed and quantified separately. The overall VfM assessment considers all of the impacts taken together, recognising their different nature. Although all of these impacts can, in principle, be expressed in monetary terms, they should not simply be added together, given fundamental differences in the certainty, timing and nature of these impacts. Moreover, the impacts will materialize over a long period of time. For example, certain tax rebates contained in the NRA Agreement can last up to 40 years. The analysis, therefore, needs to take account of the social rate of time preference (i.e. the fact that a dollar today is worth more than a dollar in say 40 years). The VfM assessment expresses all values in terms of their net present value ("NPV") as at December 31, 2011, in order to enable the comparability between NPV amounts.

The NPV date at December 31, 2011 was determined when PwC was hired by CIG in March 2012. Although more than a year has passed since that time, PwC has not changed the NPV date in order to remain consistent with earlier draft versions of this report.

Further, PwC's consideration of VfM and potential alternatives to the NRA Agreement is based solely on the conditions in place at 31 December 2011, adjusted for the impact of the subsequent three Amendments.

Unless otherwise stated, all amounts in this report are presented in United States dollars in present value terms.

1.4. Report structure

This report is set out in nine sections. Following the current Section 1, Section 2 provides a description of the NRA Agreement which is the basis of the VfM assessment. Section 3 analyzes the NRA Agreement from DRCL's perspective and considers the likely tourism and real estate development scenarios whether or not the NRA Agreement is in place.

Section 4 assesses the value of the financial components arising as a result of the NRA Agreement while Section 5 deals with the economic and social impacts. The risk-related components are addressed in Section 6.

Alternatives for CIG to finance the construction of road infrastructure are analyzed in Section 7 while Section 8 analyzes the NRA Agreement's compliance with the FFR.

Finally, PwC's overall assessment of the NRA Agreement VfM and a number of recommendations are presented in Section 9.

2. Description of the NRA Agreement

2.1. Background of the NRA Agreement

As noted in Section 1, the terms included in the NRA Agreement were initially developed as a component of the FCIA, a broader agreement between CIG and DRCL. The negotiation of the FCIA, which includes relatively complex infrastructure proposals, is ongoing at present. As such, the NRA Agreement was finalized as a stand-alone agreement, in order to allow for faster mobilization of tourism development and infrastructure projects and therefore accelerated delivery of expected economic benefits.

The NRA Agreement principally focuses on property and infrastructure located in the Seven Mile Beach corridor, including substantial DRCL land holdings adjacent to the West Bay Road and alongside the route of the ETH Extension. DRCL, together with its affiliates, is the most significant inward investor into the Cayman Islands in recent years and, in January 2011, DRCL acquired the bulk of the relevant land parcels from Fourth Quarter Properties Limited, a company owned by Stan Thomas, with a view to future development. Following this acquisition, DRCL commenced discussions with CIG with the aim of enhancing development potential of the properties, in particular through closure of a portion of WBR in order to provide viable hotel development opportunities.

2.2. Brief description of the overall NRA Agreement

The NRA Agreement's primary purpose, from CIG's perspective, is to deliver new road infrastructure and stimulate the Cayman Islands economy by encouraging investment by DRCL, particularly in the tourism sector. To this end, the NRA Agreement calls for an exchange of land and land related benefits between CIG and DRCL as well as tax rebates and waivers conceded to DRCL. The NRA Agreement can be divided into three major components:

Infrastructure and SMB Hotel development

The NRA Agreement's most important component is the closure by CIG of a portion of the WBR from approximately Governor's Way to Yacht Drive, with most of the land vesting to DRCL following the process set out in the Roads Law. In return, DRCL has extended the ETH to Yacht Drive in order to replace the portion of WBR which is to be closed and is extending the ETH to Batabano Road. DRCL will also extend the ETH to Reverend Blackman Drive. DRCL will vest all of its land required for these new roads to CIG in addition to paying compensation for any third-party land which needs to be acquired for this road construction.

Because of expected higher traffic volumes on the ETH following completion of its extension to Batanabo Road, the portion of the ETH which is a two lane road from the Bank of Butterfield Roundabout ("BOBR") to the Limestone Roundabout ("LSR") will be expanded into a four lane divided arterial road at DRCL's expense.

The purpose of closing a portion of WBR is to make DRCL's land holdings in the area more suitable for hotel and related development by providing improved access to Seven Mile Beach. DRCL property in this area includes the former Courtyard Marriott. As part of the NRA Agreement, DRCL commits to refurbishing or reconstructing and reopening this hotel ("Seven Mile Beach Hotel" or "SMB Hotel"). DRCL will also receive a 100% reduction in all development fees and import duties related to the works leading to the reopening of the SMB Hotel.

Based on a similar rationale, the NRA Agreement also calls for the eventual closure of the Old Barkers Road to provide DRCL with more suitable hotel development opportunities. The land where the Old Barkers Road is located will be vested in DRCL following the road closure for parcels where DRCL owns adjacent parcels. DRCL will in turn fund the costs of the construction by the NRA of a New Barkers Road.

In addition, DRCL made a $5m payment to CIG for educational, community and training program purposes and, following completion of the other infrastructure elements of the NRA Agreement, DRCL shall transfer five separate land holdings to public ownership for recreational and community purposes, and construct new public beach facilities at its expense, up to a maximum of $3m.

Stamp duty, development fees and import duty abatements and SMB Hotel Tax Rebate

The NRA Agreement also provides DRCL with stamp duty, stamp duty on leases, development fee and import duty abatements relating to any DRCL development, except for the SMB Hotel (which has a separate waiver under the NRA Agreement) as was as a 50% rebate of all taxes levied pursuant to the Tourist Accommodations (Taxation) Law (the "Hotel Tax Rebate") at the SMB Hotel for the first ten years following its opening, up to a net present value ("NPV") of $52.95m ("$53m Abatements"). The NPV is calculated using a discount rate of 10%. Except for the SMB Hotel Tax Rebate, there is neither a time limit applied to these abatements nor any detailed specifications relating to the type of development or their location in the Cayman Islands. However, development adjacent to the closed portion of the WBR is to be predominantly hotel/tourist resort-oriented, and stamp duty on leases at the Camana Bay development is excluded.

Hotel tax rebate for other hotels

The NRA Agreement also provides DRCL with the Hotel Tax Rebate for all of its other properties other than the SMB Hotel but without the limitation of the NPV calculation. This Hotel tax Rebate is available for a period of 10 years after a hotel is developed, redeveloped, renovated or refurbished by DRCL within 30 years of the date of the NRA Agreement.

The NRA Agreement also contains a number of other rights and benefits for both CIG and DRCL. A summary of the key terms of the NRA Agreement is provided in Appendix C.

3. Potential impact of the NRA Agreement – alternative scenarios

3.1. Introduction

In considering the implications and impacts of the NRA Agreement, it is important to compare the expected outcomes with the NRA Agreement with what is expected to happen without the NRA Agreement. As part of its analysis, PwC therefore considered how DRCL can be expected to respond to the NRA Agreement focusing, in particular, on how DRCL's plans for development in the Cayman Islands would evolve 'with the NRA Agreement' and 'without the NRA Agreement'. Two pairs of alternative scenarios have been developed following discussions with CIG and DRCL:

- With NRA Agreement:
  - Development of SMB Hotel only – **Scenario 1**;
  - Development of SMB Hotel and other real estate developments by DRCL – **Scenario 2**;
- Without NRA Agreement:
  - No development – **Scenario 1a**; and
  - Limited but delayed real estate developments – **Scenario 2a**.

The rationale and nature of each of these scenarios is explained in more detail below.

3.2. With NRA Agreement

This part of the Section describes the two scenarios that have been developed to show potential outcomes the NRA Agreement.

3.2.1. Scenario 1 – Development of SMB Hotel only

PwC's base case scenario (**Scenario 1**) assumes that DRCL will make all the planned changes to the road infrastructure described in the NRA Agreement (refer to Section 2) and then develop only the SMB Hotel in line with the conditions within the NRA Agreement: this would see an immediate investment in the road infrastructure followed by the redevelopment of the SMB Hotel as a 4/5 star hotel with an estimated 245 rooms so that it is operational and, possibly, the provision of an estimated 40 condominiums on the same site with construction starting within 12 months of the date of the NRA Agreement.

3.2.2. Scenario 2 – Development of SMB Hotel and DRCL Development Plan

PwC's alternative scenario with the NRA Agreement (**Scenario 2**) assumes that DRCL will undertake the road infrastructure developments and redevelopment of the SMB Hotel and that this will be followed by other real estate developments in land parcels which benefit from the improved access and commercial return resulting from the WBR and Barkers Road closures and the ETH Extension.

According to DRCL, it has not defined the parameters of these further real estate developments with any precision. Initially, DRCL suggested that for the purpose of the Independent Review, PwC could assume that DRCL would undertake the development of two additional hotels:

- A 200 room 4/5 star hotel along with 25 condominiums; and
- A second 200 4/5 star room hotel but this time with 50 condominiums.

The potential timing and nature of these additional investments were not defined at that time.

Subsequently, following further discussion to clarify DRCL's development plans, DRCL provided PwC with its 'theoretical development programme' which outlines more extensive plans for the construction of further hotels, condominiums, housing and office/retail space over a period of over 25 years (the "DRCL Development Plan"). All the proposed development is either in the WBR parcels or adjacent to the ETH Extension. As such, it does not include any development at Camana Bay. The DRCL Development Plan was provided to PwC in May 2012. For the purposes of this final report, PwC reconfirmed with DRCL in April 2013 that the parameters of the DRCL Development Plan remain valid, albeit commencement and completion dates will be impacted by the delays in the completion of the amendments to the NRA Agreement.

Figure 1 provides details of the five hotels in the DRCL Development Plan. It includes the SMB Hotel (also referred to by its lot number, 11B83). The WB Hotels 2-4 are all situated on the WBR parcels whilst the eco-tourism venture could be either at Barkers or in the land adjacent to the ETH, but on the North Sound water side of that land. These plans imply that the number of hotel rooms in the Cayman Islands would increase by 53% compared with 2011. They are therefore predicated on the assumption that there will be sufficient US and other international demand for the additional hotel accommodation as well as adequate air transport capacity. The ability of US and other international tourism demand to sustain this level of growth creates fundamental uncertainties regarding the deliverability of the projected timeline for hotel development: current economic trends suggest the plans are challenging. If some of the ongoing large scale development initiatives in Cayman transpire, such as the Shetty Hospital and the Cayman Enterprise City, this could support the projected capacity growth, albeit it should be noted these developments and associated hotel / real estate demand are not predicated on the NRA Agreement. Similarly, the Cayman Islands' air transport capacity represents an existing obstacle to this level of tourism growth. As such, this build out plan would likely also be predicated on the planned, but delayed, redevelopment of the Owen Roberts International Airport taking place in the next two to three years. PwC understands that the Shetty Hospital agreement includes provision for airport upgrade as a pre-requisite to the full development plans.

Figure 1
Hotel developments included in the DRCL Development Plan

	Start	End	Cost / key (excl. land) ($'000)	# keys*	Dev. cost (excl. land) ($m)	Expected ADR	Stabilised occupancy
SMB Hotel (11B83)	Jun-12	Jun-14	$272.5	265[4]	$72.2	$400	65%
WB Hotel 2	Dec-15	Dec-17	$300.0	300	$90.0	$300	70%
WB Hotel 3	Mar-15	Nov-16	$200.0	150	$30.0	$200	75%
Eco-Tourism	Apr-16	Dec-17	$225.0	100	$22.5	$350	65%
WB Hotel 4	Apr-20	Apr-22	$250.0	200	$50.0	$250	70%
Total				1,015	$264.7		

Source: DRCL
** 'Key' refers to hotel rooms*

The dates shown in Figure 1 were provided by DRCL in April 2012 when the initial version of this report was prepared. Because it has taken longer than expected to finalise the NRA Agreement and the Independent Review, work on the SMB Hotel has been delayed. According to DRCL, it plans on starting work on the SMB Hotel very soon after the Independent Review is completed, with work been carried out in the same timeframe. In fact, DRCL has started dismantling the former Courtyard Marriott building in preparation of building the SMB Hotel.

Figure 2 shows DRCL's planned developments of condominiums over the period up to 2026. All of these condominium developments are situated by the proposed hotels. Again, the scale of the development, at 425 units in total, can be contrasted with the Cayman Islands' existing stock of nearly 2,847 apartments in 2011.

[4] The 265 keys assumes a 245 key SMB Hotel with 20 condominiums (i.e. the average of the two options presented by DRCL).

Figure 2
Condominium developments included in the DRCL Development Plan

	Start	End	Cost / unit (excl. land) ($'000)	# units	Dev. cost (excl. land) ($m)	Avg. sales/unit ($'000)
WB Lands Condo 1	Jun-13	Dec-14	$660	100	$66.0	$800
WB Lands Condo 2	Jun-15	Dec-16	$1,055	50	$52.8	$1,200
WB Lands Condo 3	Jun-18	Dec-19	$1,100	100	$110.0	$1,200
WB Lands Condo 4	Sep-20	Mar-22	$700	75	$52.5	$800
WB Lands Condo 5	Jul-24	Jan-26	$800	100	$80.0	$900
Total				425	$361.3	

Source: DRCL

Figure 3 indicates the scale of the housing developments envisaged by DRCL along the ETH Extension (excluding the WBR areas). On average, this is equivalent to a rate of development of about 10% of that achieved in the Cayman Islands as a whole over the five years up to and including 2010.

Figure 3
Housing developments included in the DRCL Development Plan

	Acres (est.)	Avg. dwelling units / acre	Start	End	Cost / unit (excl. land) ($'000)	# units	Dev. cost (excl. land) ($m)	Avg. sales/ unit ($'000)
Crymble Landholdings	419	2.0	Jun-14	Jun-39	$1,000	838	$838.0	$1,100
CIYCAM Lands	57	3.0	Mar-15	Mar-23	$800	171	$136.8	$900
Total	476					1,009	$974.8	

Source: DRCL

Finally, **Figure 4** shows the development of office / retail space DRCL anticipates. These are seen essentially as ancillary commercial developments to support the resorts and housing development.

Figure 4
Office / retail developments included in the DRCL Development Plan

	Start	End	Cost / RSF (excl. land) ($)	RSF	Dev. cost (excl. land) ($m)	Starting rent / RSF ($)	Initial annual rent ($m)
Commercial Ctr 1	Jun-15	Dec-16	$470	50,000	$23.5	$45	$2.25
Commercial Ctr 2	Jun-19	Dec-20	$470	50,000	$23.5	$45	$2.25
Total				100,000	$47.0		$4.50

Source: DRCL

PwC has not attempted to corroborate or form a view on the projected returns to DRCL resulting from the DRCL Development Plan outlined above as it is outside of scope of this Independent Review. PwC did note, however, that, on the face of it, DRCL's projected returns from real estate development and hotel operation appear low. As such, even allowing for the fact that as a private investor DRCL does not have to meet the short term profitability expectations of public shareholders, it seems likely that the hotel and real estate pricing and/or cost estimates would have to be further developed in the future in order to deliver more viable returns.

3.3. Without NRA Agreement

In order to understand the net impact of the NRA Agreement, it is important to consider how development of the Cayman Islands hospitality sector, and the real estate sector more generally, would develop 'without the NRA Agreement'. Specifically, consideration must be given to whether any of the development would take place at the same time and on the same scale 'without the NRA Agreement' and, if so, which investment would be likely to occur – not necessarily by CIG and/or DRCL – at some point in the future. PwC has, therefore, sought to assess the likely responses of the different stakeholders in such a situation (i.e. without the NRA Agreement).

Based on PwC's analysis (see Section 4.2.6), PwC believes that there are good reasons why the redevelopment of the SMB Hotel is reliant on changes being made to the road infrastructure, specifically the closure of WBR, so that guests at the SMB Hotel will be able to enjoy direct access to the beach. Previously, the SMB Hotel has failed on two occasions, with the lack of direct beach access being cited as an important contributory factor. Significantly, all the other major hotels along SMB have direct beach access, for example the Ritz-Carlton, the Westin and the Marriott. In this respect, the former Holiday Inn/Courtyard Marriott (where the SMB Hotel will be located) was at a distinct disadvantage compared to others. It is also notable that according to the report prepared for DRCL by REVPAR International (the "REVPAR Report"): "Once West Bay Road is eliminated, Site 11B83 (the SMB Hotel) will arguably offer one of the best beach experiences/scenes on Grand Cayman."[5]

From discussions with the NRA, it is clear that the planned changes to the road infrastructure would not take place on the same scale without the NRA Agreement:

- Extension of the ETH would not be affordable for as long as the existing pressure on the CIG's public finances remains and the obligation to abide by the principles of the FFR exists; and
- Closure of WBR would not be a priority and, indeed, it is unlikely that it would be pursued at all in the absence of the NRA Agreement.

This means that it is quite plausible that the SMB Hotel will only be developed with the NRA Agreement and that 'without the NRA Agreement' DRCL would make no investment in renovating and redeveloping the SMB Hotel.

This does not necessarily mean, however, that no other hotel developments would be undertaken in the Cayman Islands, either by DRCL or by another developer. Evidence provided by DRCL indicates that one of their advisers – REVPAR International – expects significant investment in additional hotel capacity in the Cayman Islands in the period through to 2020[6]. The key question, therefore, is whether DRCL or indeed any other developer might reasonably be expected to invest in additional hotel capacity over and above that envisaged by REVPAR in the absence of the NRA Agreement.

PwC has reviewed the developments outlined in the DRCL Development Plan with a view to assessing the likelihood that some or all of them would occur at some point in time in the future without the NRA Agreement. This review suggests that:

- Since the WB Hotels 2-4 are all situated on the WBR parcels, they would probably not be viable without the WBR closure and would, therefore, be unlikely to proceed without the NRA Agreement.
- Whilst the eco-tourism venture would not go ahead immediately without the NRA Agreement, it would probably go ahead at some point in time in the future (when the ETH Extension is built).
- By virtue of their location close to the WBR hotels, the condominiums are linked to the WBR closure but do not completely depend on it.
- If the ETH Extension (only) were to be built in say ten years time, then the housing development would go ahead in some form.
- The office/retail developments depend on whether the hotels, condominiums and housing are developed on the proposed scale.

It must be noted that DRCL started construction of the ETH Extension in early 2012, soon after the initial NRA Agreement was signed. At the time of this report, Phase 1, to the new roundabout at Yacht Drive, is complete and the road has been opened while Phase 2, to Batabano Road including the extension to Reverend Blackman Drive, is well advanced **[To update before final report issued]**. However, it is unclear what would happen if the NRA Agreement were terminated. According to the NRA Agreement, should the NRA Agreement be terminated by DRCL for breach by CIG, CIG would be liable to compensate DRCL for the cost of constructing the ETH Extension as well as other costs. Presumably, following such a settlement, CIG could take possession of the ETH Extension, complete any outstanding work and open it to public use. However, delays are possible before a settlement were to be reached, and given CIG faces considerable financing constraints this could potentially further delay opening of the ETH Extension. Furthermore, as noted in Section 1.3, PwC's approach

[5] Lodging Market Review Grand Cayman, prepared by REVPAR International for DRCL, December 21, 2011, page 11
[6] Lodging Market Review Grand Cayman, prepared by REVPAR International for DRCL, December 21, 2011, page 22

is to consider VfM at the time of the original NRA Agreement, 31 December 2011, at which point the road construction had not commenced. PwC has therefore maintained the assumption of a ten year delay in opening the ETH Extension, and subsequent real estate development, in under a 'without the NRA Agreement' scenario.

On this basis, PwC has developed two alternative scenarios which describe what might happen 'without the NRA Agreement' (i.e. the so-called counterfactual scenario).

3.3.1. Scenario 1a – No development of SMB Hotel

The simplest counterfactual scenario (**Scenario 1a)** assumes that DRCL would not undertake redevelopment of the SMB Hotel nor would it undertake any of the other developments included in the DRCL Development Plan for the 20 year period covered by PwC's appraisal.

3.3.2. Scenario 2a – Limited development of DRCL Development Plan

The alternative counterfactual scenario (**Scenario 2a**) assumes that DRCL would undertake some of the projects in the DRCL Development Plan at some point in the future once the CIG is able and willing to fund the ETH Extension. Specifically, PwC assumes that the CIG would be in a position to finance the ETH Extension publically within ten years, and that DRCL would undertake:

- The eco-tourism venture ten years later than currently planned;
- Half of the condominium developments envisaged in the plan, but again with a delay of ten years; and
- The housing developments and office/retail development, again with a delay of ten years for both.

PwC assumes that in the absence of the NRA Agreement neither DRCL nor any other developer would undertake alternative hotel developments which would not have been viable had the NRA Agreement and its associated development been carried out.

3.4. Summary

PwC has used the two pairs of scenarios described above as the basis for analysing and modelling the implications of the NRA Agreement for the wider Cayman Islands economy. This analysis is presented in Section 5 following an analysis of the NRA Agreement's financial impact in Section 4.

4. Assessment of implications of the Agreement for the public finances

4.1. Introduction

This section presents the financial analysis of the NRA Agreement based on the three major components set out in Section 2, namely:

- Infrastructure and SMB Hotel development
- Stamp duty, development fees and import duty abatements; and
- Hotel Tax Rebate.

This analysis is part of the overall VfM assessment and its results must be considered in conjunction with the economic analysis (Section 5) and risk analysis (Section 6).

The financial analysis has a horizon of 40 years, from 2012 to 2052. This 40 year period corresponds to the potential duration of the Hotel Tax Rebate, which is available for ten years for **hotel openings or renovations** occurring within 30 years of the execution of the NRA Agreement. It is therefore possible that CIG will be providing DRCL with the Hotel Tax Rebate until 2052.

To make all amounts comparable, they have been expressed in terms of their NPV as at January 1, 2012 using a discount rate of 3.5% (with the exception of cash flows eligible to the $53m Abatements that have been discounted using 10.0% rate, as per the NRA Agreement). This discount rate is taken from CIG's FFR. PwC understands that this 3.5% rate is before inflation. When amounts are inflation adjusted, an annual inflation rate of 2.0% has been used. When applied against inflation adjusted amounts, the discount rate is adjusted to 5.5%, which broadly approximates to the CIG's current cost of capital.

Accordingly, as noted earlier, all amounts in this section are expressed in US dollars at their NPV value unless otherwise noted.

4.2. Infrastructure and SMB Hotel development

This component comprises a large number of benefits received by CIG from DRCL and corresponding CIG costs and divestments of property and/or future tax levies. These benefits, costs and divestments are summarized in **Figure 5**.

Figure 5
Components of infrastructure and SMB Hotel development

Benefits to CIG	CIG Costs and Divestments
1. ETH Extension construction	2. NRA monitoring of ETH Extension and New Barkers Road construction
3. New Barkers Road construction	4. Additional NRA operating costs of ETH Extension
5. Land required for ETH Extension provided by DRCL	6. WBR closure land vested to DRCL and subsequent DRCL land value uplift
7. Land required for ETH Extension purchased from third parties and paid for by DRCL	8. Old Barkers Road closure land vested to DRCL and subsequent DRCL land value uplift
9. Land required for New Barkers Road provided by DRCL	10. SMB Hotel development fees and import duties rebate

Benefits to CIG	CIG Costs and Divestments
11. Value uplift of CIG lands subsequent to ETH Extension	12. Import duties waiver for public infrastructure constructed by DRCL
13. Cash grant paid by DRCL to CIG	14. Existing and required public rights of way to the sea along WBR extinguished
15. Land for New Public Beach	16. Additional NRA operating costs of ETH Expansion
17. Leasehold interest in Soto Land	
18. New Public Beach and Public Beach Park development costs	
19. West Bay pedestrian and bicycle paths	
20. Land and access road for Sunrise Adult Training Centre	
21. Land for educational and community purposes and for a cemetery	
22. Land at Smith's Cove	
23. ETH Expansion construction	

Each of these benefits, costs and divestments is analyzed separately below. The NRA Agreement also provides for other benefits to CIG (such as DRCL providing CIG with land, for no compensation, to build a roundabout at ETH and Batabano Road should the NRA build such a roundabout) and other benefits to DRCL (such as the right for DRCL to install conduits under the ETH Extension that DRCL could licence for a fee to utility providers). Since these potential benefits are not considered material in the context of VfM, they have not been analyzed.

Since one of the purposes of the Independent Review is to assess the NRA Agreement value to the Cayman Islands, **benefits provided by CIG to DRCL are analyzed from the perspective of their cost to (or value forgone by) CIG and not in terms of their potential value to DRCL.**

4.2.1. ETH Extension construction

DRCL is responsible for the design and construction of the ETH from Raleigh Quay to Batabano Road, including the extension of Reverend Blackman Drive from the ETH to Willie Farrington Road (together, the "ETH Extension") at its sole cost and expense.

PwC mandated JEC to estimate the cost of constructing the ETH Extension using information provided mainly by DRCL, including engineering drawings and estimate of quantities. This cost estimate is based on quantities and unitary prices (including labour), and excludes any risk provisions which are estimated in Section 6. At the date of this report, design of the ETH Extension is complete, construction of Phase 1, to the new roundabout at Yacht Drive, is complete and completion of Phase 2, to Batabano Road including the extension to Reverend Blackman Drive, is expected by May 2013 **[to be updated before final report issued]**. JEC based its cost estimate on the ETH Extension's state of design and construction as at April 2012, the date of its report. PwC understands from DRCL that, as at April 2013, no unexpected events have occurred or technical conditions been encountered by DRCL that have had a material impact on the budgeted costs for the ETH Extension.

DRCL's design for the ETH Extension includes culverts and possible bridges required for access to DRCL land parcels. These additional works are excluded from JEC's cost estimate on the basis that the works are not driven by public infrastructure needs but are instead required for private development purposes.

JEC's estimate for the construction cost is $37.3m. Details of JEC's estimate are provided in **Appendix E**.

4.2.2. NRA monitoring of ETH Extension and New Barkers Road construction

The NRA is responsible for monitoring the construction of the ETH Extension and New Barkers Road to ensure DRCL meets the design and quality standards set out in the NRA Agreement. The NRA expects to perform various quality control activities, design development supervision and construction supervision during construction of these roads by DRCL and its subcontractors. Based on its experience, the NRA estimates its monitoring costs at 2% of related construction costs.

PwC understands from the NRA that, as at April 2013, its actual monitoring costs to date for the ETH Extension are in line with its initial expectations.

Based on this assumption and the estimated construction cost, plus additional risk estimates (Section 6), for the ETH Extension and New Barkers Road, NRA monitoring costs are estimated at an NPV value of $0.8m.

4.2.3. New Barkers Road construction

The NRA Agreement provides for the eventual closure or realignment of the Barkers Road, principally in order to facilitate future tourism development by DRCL of its waterfront land in this area. Clauses 83 – 86 of the original NRA Agreement included a requirement for DRCL to construct a replacement public road, in this area, the 'New Barkers Road', as a pre-requisite for the closure of the existing public road. As per the Second Amendment, DRCL's obligations following the closure of the Barkers Road are only to:

> *"accommodate and assist with providing public access to the Barkers National Park."*

When questioned about the specifics of this obligation, DRCL replied that it intends to provide a replacement New Barkers Road on the same basis as outlined in the original clauses 83-86 of the NRA Agreement. This undertaking is further supported by clause 41 of the Third Amendment. We have therefore assumed that a New Barkers Road will be provided by DRCL. However, we also outline a related risk in Section 6.2.10.

According to the original NRA Agreement, DRCL is responsible for the design and construction of the New Barkers Road at its sole cost and expense. However, under the Third Amendment, the NRA now appears to be responsible for carrying out these works, with DRCL agreeing to reimburse the NRA for its construction costs.

The planned road is expected to be simple, with a chip and spray surface and no curbs, gutters or islands. Similarly to the ETH Extension, PwC mandated JEC to estimate the cost of constructing the New Barkers Road.

DRCL's design for the New Barkers Road is at a preliminary stage, and detailed plans and surveys are not available. As a result JEC's estimate for the construction cost is necessarily preliminary and subject to potentially significant variance. JEC's initial estimate for this cost it $1.2m and includes provision for additional fill for widening and raising the existing ground. DRCL has highlighted there may be some uncertainty in the NRA Agreement as to which party is required to meet the costs of this initial groundwork. Details of JEC's estimate are provided in **Appendix E**.

4.2.4. Additional NRA operating costs of ETH Extension

Upon its completion, the NRA will be responsible for operating and maintaining the ETH Extension. Since the NRA will no longer be required to operate and maintain a portion of the WBR following its closure, the additional cost incurred for operating the ETH Extension must be estimated net of WBR operating costs no longer incurred.

According to the NRA, the ETH Extension will likely be less costly to maintain on a comparable square footage basis than the portion of the WBR which is to be closed, in particular because of less sand cleaning and reconstruction after storms. Overall, the NRA estimates that the cost of maintaining the longer stretch of ETH Extension will be similar to the cost no longer incurred for maintain the closed portion of the WBR except for

additional grass cutting along the ETH's median and shoulders. The NRA estimates the additional costs at approximately CI $56,000 per year.

The NRA Agreement provides DRCL with a licence permitting DRCL to maintain landscaping along a portion of the ETH. Should DRCL exercise this right, the NRA's road maintenance costs will likely decrease.

The ETH Extension will have a higher operating cost than the WBR because of additional lighting which is required as well as maintenance of an overpass.

The NRA estimates the additional lighting costs (measured at the standard rate for public lighting) at approximately CI $150,000 per year. DRCL is responsible for any additional operating costs resulting from the installation of enhanced road lighting which it may decide to have installed.

The ETH Extension will include a concrete overpass comprising a precast reinforced concrete arch and vertical reinforced concrete walls. According to an estimate prepared for DRCL by Apec Consulting Engineers Ltd, this overpass will require washing every two years at a cost of CI$23,000 and painting every ten years at a cost of CI$263,000.

In total, this represents a total cost for the NRA of $5.9m in NPV value over the 40-year analysis horizon.

4.2.5. Land required for ETH Extension provided by DRCL

DRCL will transfer to CIG approximately 32.94 acres of West Bay land currently in DRCL's ownership required to construct the ETH Extension. Upon the execution of the NRA Agreement, DRCL waived any right to compensation it may have under applicable laws and regulations.

DRCL claims that the foregone compensation resulting from its waiver represents $23.2m. According to DRCL, such compensation would be caused mostly because of severance, meaning the separating of its lands from one large continuous lot into two lots separated by the ETH. DRCL believes this severance reduces its ability to undertake certain large scale development on its West Bay lands. However, DRCL did not provide PwC with calculations supporting a compensation figure.

CIG's Department of Lands and Surveys ("DLS") estimates that the construction of the ETH Extension will have an overall positive effect on DRCL's West Bay land by providing improved access and thus facilitating their development. DLS informed PwC that it values the net uplift in value of DRCL's West Bay lands at a minimum of $8m. However, DLS did not provide PwC with its detailed calculations.

The true impact of the ETH Extension on DRCL's West Bay lands is difficult to estimate since DRCL does not have a well established development plan for these properties. While PwC does acknowledge DRCL's reasoning concerning severance, construction of the ETH Extension would appear to be beneficial to the development potential of the West Bay lands, and it should be noted that the proposed ETH Extension was known to DRCL in January 2011 at the time it purchased the land parcels. Accordingly, no value has been attributed to any compensation payable to DRCL by CIG. On the other hand, no value uplift has been attributed to DRCL lands for the purpose of the Independent Review since DLS has confirmed that it is unlikely that CIG would have any grounds to claim a portion of any such uplift from DRCL under normal circumstances.

4.2.6. WBR closure land vested to DRCL

The purpose of the WBR closure is to provide direct beach access to DRCL's lands, including the SMB Hotel, which are currently on the east side of the WBR. The closure is being carried out to facilitate DRCL's hotel development, rather than for any public infrastructure purposes. As such, the WBR closure and land vesting in DRCL represents a divestment of a public asset, for which CIG should ensure reasonable sale proceeds are achieved.

DRCL owns a number of small lots on the west side of the WBR (that is, on the beach side) as well as a number of much larger lots on the east side of the WBR. DRCL's west side lots have limited development potential because of their size whereas the east side lots are not suitable for hotel development because of their lack of

beach access. The two hotels which previously operated on the location of the planned SMB Hotel, the former Holiday Inn and the Courtyard Marriott, both failed, with the lack of direct beach access being cited as an important contributory factor. Significantly, all the other major hotels along Seven Mile Beach, for example the Ritz-Carlton, the Westin and the Marriott, have direct beach access. The REVPAR Report observed that: "Once West Bay Road is eliminated, Site 11B83 (the SMB Hotel) will arguably offer one of the best beach experiences/scenes on Grand Cayman."[7]

Although the land under the portion of WBR which is to be closed has practically no fair market value on its own, irrespective of its replacement value to CIG, closure of WBR does significantly increase the value of DRCL properties located on either side of the WBR. According to a valuation report prepared by Integra Realty Resources on behalf of the DLS, the value of DRCL's WBR properties will increase by CI$98.3m following the closure of the WBR.[8] This conclusion is supported by a valuation prepared in-house by DLS which estimates the value increase at CI$91.0m[9].

DRCL commissioned its own independent valuation report, prepared by Charterland Ltd[10]. According to this report, when corrected for certain mathematical inaccuracies, the value of DRCL's WBR properties will increase by CI$70.5m following the closure of the WBR. DLS disputes this conclusion, arguing that Charterland inappropriately used comparable sale data calculated on a linear foot basis instead of on a square foot basis[11]. Because different parcels of land have varying depths, DLS contends that the linear foot basis leads to discrepancies which are avoided by using a square foot basis. Also, DLS contends that Charterland did not consider the value to DRCL of its various lots being developed as a whole instead of on a lot by lot basis. DLS believes that by not considering this marriage value, the value uplift is underestimated. Finally, DLS states that the Charteland report omits the uplift on parcel 11B82, which is immediately behind DRCL's beachfront parcel 11B83 and which will increase in value by being developed as part of a larger beachfront property following the closing of the WBR.

Although DRCL was provided with the IRR report it has not provide any comments on its methodology or conclusions.

For the purpose of the Independent Review, the DLS estimate of CI$91.0m has been adopted since it is broadly in line with the independent valuation prepared by Integra Realty Resources (CI$98.3m) and has less divergence from the lower valuation prepared by Charterland (CI$70.5m).

Under the terms of the NRA Agreement, DRCL must provide a thirty foot private vehicular right of way in favour of unaffiliated property owners immediately adjacent to the closed portion of the WBR. In practice, this means DRCL will be obliged to construct an access road to parcels 10E11 and 10E33 (the Lenham Properties) and 10E37 (the Sundowner condominiums). Based on the likely initial route of this access road along the closed section of WBR and indicative road cost per linear foot, DRCL has estimated a likely cost for this access route of CI$0.2m. This cost reduces DRCL's value uplift to CI$90.8m. PwC notes that DRCL will be obliged to construct a second, more costly access road, leading inland over unfilled marshland in order to fully develop its inland parcels 10E36 and 10E47 in the future. However, neither DRCL nor DLS are able to provide an estimate for this additional cost to DRCL at this stage.

This CI$90.8m value uplift accrues entirely to DRCL at no direct cost to CIG. However, since this value uplift can only be gained by DRCL because of the WBR closure by CIG, CIG can legitimately claim a share of the uplift. Indeed, in a standard disposal transaction a rational seller would insist on a share of this value. The UK HM Treasury's Green Book[12] provides guidance on valuing benefits and costs where there is no readily

[7] Lodging Market Review Grand Cayman, prepared by REVPAR International for DRCL, December 21, 2011, page 11
[8] Analysis of Proposed Roadway Changes Revision 3, prepared by Integra Realty Resources-Caribbean for DLS, 25 February, 2013
[9] Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013
[10] Valuation: Land Used as Road re: West Bay Road Closing, prepared by Charterland Ltd for DRCL, 9 January, 2013
[11] Report on review of Charterland Valuation on the Closure & vesting of West Bay Road (Part), prepared by DLS, 15 March, 2013
[12] HM Treasury Green Book, Appraisal and Evaluation in Central Government 2011, page 23

determinable market value through a process of determining willingness of the counterparties to pay for a benefit.

In the case of a potential transaction where there is only one possible buyer and only one possible seller with the ability to carry out the transaction, assuming each has an equally strong negotiating position, the negotiated price should be the median value between the seller's value and the buyer's value. In the current case, the "value" of the WBR lands uplift to CIG is nil since it does not own these properties. The value to DRCL is CI$90.8m as explained above. The remaining question is how to split the value between the two parties. PwC believe that, in the absence of any evidence to the contrary, it should be assumed that CIG and DRCL have equal bargaining power and neither is more compelled to act than the other. In such a situation, the most reasonable approach is to assume a 50:50 sharing of the uplift, that is, the mid-point between the two values..

This approach has been used by the CIG when its actions create value for a private party. An example of this is DLS' practice when extending a lease for CIG land. In such cases, DLS will calculate the notional value of the lease extension. Since the lease extension does not represent a "cost" for CIG, it will usually require the tenant to make an upfront payment at least equal to a minimum of 50% of the lease extension value. It is noted that both DLS and DRCL believe that CIG and DRCL respectively have the greater bargaining power. DLS believes that CIG has a stronger bargaining power than DRCL because of the substantial amounts that DRCL has invested in acquiring land along the WBR, including certain parcels at, in DLS's opinion, higher than market value. However, DRCL has shown itself to be a long-term investor which is willing to acquire land and wait many years before undertaking its development.

In their valuation report, Integra Realty Resources were asked by DLS to comment on what percentage of net value uplift to DRCL should be paid to CIG, assuming the payment was in cash and solely for compensation for closure of the WBR. Integra Realty Resources noted that the 'compromise' figure will largely reflect relative bargaining power of the parties and highlighted DRCL's strong motivation to execute the transaction. Integra Realty Resources concluded that a 50% split of the uplift value is the only number that there is evidence to support, and cited the historical approach of the UK Leasehold Valuation Tribunal in support of this. Charterland, it its report, takes a similar position, stating that "a 50:50 split is generally considered to be the norm unless other circumstances are known".

DRCL has expressed its disagreement with this approach. In particular, it believes that it has no legal obligation to pay CIG for any portion of the value uplift which could result from a road closure. PwC does not have any opinion on the legal aspects of this matter as this is beyond our brief. PwC's analysis in this respect is predicated on the assumption that CIG was free to enter into, or not enter into, the terms of the NRA Agreement based on its own assessment of the commercial terms as a whole. Accordingly, we are of the opinion that the value uplift accruing to DRCL must be taken into consideration in the VfM assessment which is at the heart of the Independent Review. Without the improved real estate potential of DRCL's properties along the WBR following the road's closure, as expressed by the value uplift, the NRA Agreement makes no commercial sense to DRCL. PwC's inclusion of the value uplift in its VfM assessment therefore reflects the commercial underpinnings of the NRA Agreement, not any legal requirements.

PwC believe a reasonable sharing of this uplift is $55.4m, the mid-point between the nil value of the WBR lands uplift to CIG and the CI$90.8m value to DRCL as explained above. This is the amount CIG could expect to receive from DRCL if DRCL were to "buy" the WBR from CIG. Since the CIG is not receiving cash compensation in return for the WBR closure, PwC has treated this foregone value as a cost to CIG.

Converted to its NPV value, CIG's share of the WBR lands value uplift is $55.4m. For the purpose of this analysis, this is considered a divestment of a public asset by CIG to DRCL for which a reasonable negotiated price would be $55.4 m.

To test the soundness of this conclusion, PwC considered the replacement cost of the WBR. No independent valuation has been prepared of the portion of the WBR to be closed and vested to DRCL. At PwC's request, an estimate of the replacement value of the portion of the WBR to be closed and vested to DRCL was prepared in-house by CIG. According to the NRA, the replacement value of the infrastructure (that is, the road surface and

foundation without considering the underlying land) is CI$620,000[13]. This value is low because of the age of this portion of the WBR, which was built in the 1950s, its current condition, having received its most recent layer of asphalt in 2000 and the lack of sidewalks and drainage facilities. According to DLS, the theoretical value of the underlying real estate for public accounting purposes is CI$34.5m[14]. Taken together, this represents a total replacement value of CI$35.1m of the portion of the WBR to be closed and vested to DRCL. This is equal to an NPV value of $42.8m which, while lower than the uplift value of $55.4m calculated above, broadly supports the approach taken by PwC.

4.2.7. Land required for ETH Extension purchased from third parties and paid for by DRCL

DRCL must reimburse CIG for any compensation CIG is required to pay third party owners relating to land expropriated for the ETH Extension. DRCL must also compensate CIG for any costs incurred by CIG in relation to such expropriations, such as the cost of legal proceedings.

At this stage only one related compensation claim has been received by CIG and none have been settled, however the DLS and DRCL agree that a fair estimate of all such land expropriation and related costs is CI$1.3m. This is equal to an NPV value of $1.6m.

4.2.8. Old Barkers Road land vested to DRCL and subsequent DRCL land value uplift

Upon approval being granted by the Central Planning Authority in respect of an application by DRCL for permission to develop its land in Barkers, CIG will proceed with the closure of the Old Barkers Road and vest this land to DRCL. As with the WBR closure, the Barkers Road closure is being carried out to facilitate future tourism development by DRCL, rather than for any public infrastructure purposes.

Using the same approach as for the WBR closure, PwC has not given any value to the Old Barkers Road land to be vested to DRCL but has taken into account 50% of the value uplift of adjacent DRCL land.

According to a valuation report prepared by Charterland Ltd. on behalf of the DLS, the value of DRCL's Barkers properties should increase by CI$2.8m following the closure of the Old Barkers Road.[15] This amount is slightly overstated since Charterland did not take into account that a portion of parcel 8A20 will be transferred to CIG but the difference is not considered material. This conclusion is supported by a valuation prepared in-house by DLS which estimates the value increase at CI$3.0m[16]. For the purpose of the Independent Review, the Charterland estimate of CI$2.8m has been retained since it was prepared by a third party.

Based on a 50% sharing and converted to its NPV value, CIG's share of the Barkers lands value uplift is $1.7m.

4.2.9. Land required for New Barkers Road provided by DRCL

DRCL will transfer to CIG the land required for the construction of the New Barkers Road. DRCL estimates that it could normally claim compensation of $1.2m for this land. PwC has not been provided the details of this estimation, and DLS has taken the position that no compensation would be due in light of the improved access to DRCL land holdings resulting from the New Barkers Road.

As per the Third Amendment, DRCL waives its rights for any compensation from CIG for any land it transfers for the construction of the New Barkers Road.

[13] Email from NRA to PwC, October 19, 2012
[14] Email from DLS to PwC, February 18, 2013
[15] Valuation Report: Land re. Barkers Road Closure, prepared by Charterlands Ltd. for DLS, February 20, 2013
[16] Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013

4.2.10. SMB Hotel development fees and import duties rebate

DRCL receives a 100% waiver on all development fees as well as for all import duties on materials, goods and supplies that it will import for the refurbishment of the SMB Hotel. DRCL now plans to completely rebuild the SMB Hotel, as opposed to its earlier plans to refurbish most of the existing structure. Accordingly, the entire project is subject to development fees.

This rebate is included in this part of PwC's analysis since it considered a tangible cost which will be incurred by CIG over the short term, which is directly related to the construction of the SMB Hotel, the focal point of the entire NRA Agreement, and because its cost can be calculated with a high degree of certainty. Other, less tangible costs to CIG, are analyzed separately in Sections 4.3 and 4.4 below.

DRCL has estimated the value of this foregone revenue for CIG based on the following assumptions:

- Size of SMB Hotel: 245 hotel rooms and 40 condominiums
- Development cost: $315,000 per room or approximately $90m in total
- Average development fee: $15,700 per room
- Import duties: $23,000 per room

PwC was provided with the high level DRCL calculations supporting these assumptions.

The NRA Agreement requires DRCL to start work on the SMB Hotel within 12 months of the execution date of the NRA Agreement and for work to continue until it is completed. DRCL has advised that full work on the SMB Hotel construction is now expected to commence in soon after the Independent Review is completed, with the opening provisionally scheduled for the first half of 2015. While this represents a delay in commencement of full construction relative to the original timetable, i.e. by December 2012, this delay arguably simply reflects the delays in completion of the finalised NRA Agreement, the Third Amendment to which was signed in XXXX 2013 **[to be updated]**. However, as noted in Section 6, further delays to the timetable represent a risk to the timing of economic benefits.

Overall, based on DRCL's estimates, the SMB Hotel development fees and import duties rebate is estimated to have an NPV value of $10.5m.

4.2.11. Value uplift of CIG lands subsequent to WBR closure

CIG owns adjacent land to the portion of the WBR which is to be closed, including parcels 11B23, 11B26 and 11B37. The value of this land should increase following the closure of the WBR in the same manner as the value of DRCL's land in the area will increase in value (refer to Section 4.2.6).

According to a valuation report prepared by Integra Realty Resources on behalf of the DLS, the value of CIG's lands adjacent to the WBR will increase by CI$1.7m[17] following completion of the closure of the WBR. All of this value uplift is attributed to CIG since it owns the land.

DLS disagrees with this uplift calculation. In its view, there is no uplift in the value of CIG's lands because they will be used for the planned Public Beach Park and therefore remain unavailable for private development. PwC does not agree with DLS' position; the uplift in CIG's land will occur even if CIG does not decide to monetize it.

The NPV value of this amount is $2.0m.

4.2.12. Import duties waiver for public infrastructure constructed by DRCL

The NRA Agreement provides for a 100% reduction of import duties on materials, goods and equipment imported by DRCL or its contractors in relation to the construction of public infrastructure such as the ETH Extension.

[17] Analysis of Proposed Roadway Changes Revision 3, prepared by Integra Realty Resources-Caribbean for DLS, 25 February, 2013

The impact on the VfM calculation is considered to be nil because if CIG were to build an identical infrastructure on its own, the price charged by the private contractor would be increased by the equivalent of such import duties which would then be payable to CIG. The net result is no gain or cost to CIG.

4.2.13. Cash grant paid by DRCL to CIG

DRCL has contributed $ 2.5m to CIG for a residential mortgage arrears assistance program available to qualified Caymanians and $ 2.5m for education, parks and housing projects by CIG. PwC understands that these amounts have been paid by DRCL to CIG as at the date of this report.

4.2.14. Existing and required public rights of way to the sea along WBR extinguished

According to the Cayman Islands Development and Planning Regulations, a land owner seeking permission for a hotel/tourism development on beachfront property must provide, for every 100 feet of shoreline, a minimum six foot right of way ("ROW") allowing public access to the sea from the public road. DRCL currently provides two such ROWs, one each for parcels 11B61 and 11B83. It will also normally be obliged to provide new ROWs along Seven Mile Beach should it wish to develop its WBR land.

In exchange for DRCL transferring land in Barkers for a new public beach (see Section 4.2.15), CIG will extinguish all DRCL obligations to provide such ROWs. This includes the two existing ROWs as well as ROWs relating to new developments. According to a valuation prepared in-house by DLS, this represents a total of 12 ROW, as follows[18]:

- Two existing ROWs, one each for parcels 11B61 and 11B83;
- 9 ROWs to be created along parcels 11B70 to 10E10, excluding a 12 foot ROW to be created at parcel 10E53 and at parcel 11B70;
- One ROW to be created at 10E62.

Based on a market value of CI$200 per square foot, DLS estimates the total value of these ROWs at CI$4.0m, to which it adds a 20% premium to reflect the greater development flexibility gained by DRCL because of the elimination of these ROW. This brings their final value to CI$4.8m.

DLS also instructed Integra Realty Resources to carry out an independent valuation of these ROW[18]. They arrive at a value of CI$3.0m. DLS disagrees with this value because it was calculated on a linear foot basis instead of a square foot basis. PwC has therefore retained the DLS valuation.

It is important to note that the land relating to these ROWs is not owned by CIG, but rather by DRCL, therefore a conventional sale value is not appropriate. Instead, we must infer the value forgone by CIG in waiving the ROWs.

Only DRCL can derive value from the extinguishing of these actual or potential ROWs. Since DRCL are the only potential beneficiary, PwC has applied a 50% discount to the value calculated by DLS, based on the same reasoning as set out in section 4.2.6. The value forgone to CIG of extinguishing these ROW is therefore CI$2.4m.

The NPV value of this amount is $2.9m.

4.2.15. Land for New Public Beach

DRCL will provide approximately 10 acres of beach frontage land in Barkers for the creation of a public beach ("New Public Beach"). CIG and DRCL have agreed that this land will be taken from parcel 8A19 and a portion of parcel 8A20.

[18] Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013

DLS estimates the land has a market value of CI$6.75 per square foot, which results in a market value of CI$3,000,000[19]. This is broadly in line with an independent valuation prepared for DLS by Bould Consulting Limited, which assessed the value at CI$3,300,000[20]. Another independent valuation, prepared for DRCL by Charterland Ltd, assessed the value at CI$1,960,000[21]. However, the Charterland valuation report is based on an outdated area of 7.02 acres, whereas both DLS' and Bould's valuations reflect the updated area of 10.01 acres. Given that Charterland's estimated value in US$/psf broadly correlates to that estimated by Bould, PwC had therefore relied on the Bould Consulting Limited valuation which was independently prepared and corroborated by DLS' valuation.

Accordingly, the total value comes to CI$3,300,000 and has an NPV value of $4.0m.

4.2.16. Additional NRA operating costs of ETH Expansion

The NRA believes the ETH Expansion will have essentially no additional operating costs than the existing roadway except for additional lighting costs. The NRA estimates the additional lighting costs (measured at the standard rate for public lighting) at approximately CI $40,000 per year.

In total, this represents a total cost for the NRA of $1.0m in NPV value over the 40-year analysis horizon.

4.2.17. Leasehold interest in Soto Land

DRCL will surrender to CIG its leasehold interest in parcels 11B7, 11B23 and 11B26 (known as the "Soto Land"). CIG already owns the underlying freehold for the Soto land. The Soto Land lies behind the existing public beach. Following the closing of the WBR and the transfer of the leasehold, CIG plans on developing the Soto Land as a park to complement the public beach (together the "Public Beach Park").

The Soto Land lease expires on 28 February, 2068. DRCL purchased the lease in May 2011 for CI$5,040,000.

A number of factors have an influence on the value of the Soto Land leasehold:

- Approximately 65,000 square feet of on the southern part of parcel 11B23 will be acquired by the NRA in order to build a new road linking the ETH to the WBR, thus reducing the amount of land available for either recreational or commercial development;
- A 30' ROW will be created across the Soto Lands in order to give access to DRCL's Calico Jack's beachfront restaurant, which will also restrict the commercial or recreational development potential;
- CIG intends to use the Soto Land to create the Public Beach Park, not for commercial development.

DLS estimates the leasehold interest has a market of CI$4,300,000[22]. This is in line with an independent valuation prepared for DLS by Integra Realty Resources, which assessed the value at CI$4,385,000[23]. However, an independent valuation prepared for DRCL by Charterland Ltd assessed the value at CI$7,460,000[24].

The difference between the DLS/Integra Realty Resources value of CI$4,300,000 and the Charterland value of CI$7,460,000 can be almost entirely explained by the fact that:

- Charterland does not subtract the 65,000 square feet from parcel 11B23 that the NRA will use to build a new road, which, at CI$12 per square foot, represents a value of CI$780,000; and

[19] Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013
[20] Property Appraisal, Block 8A, Parcel 19 & 20 (part only), prepared by Bould Consulting Limited Ltd for DLS, 19 February, 2013
[21] Valuation: Beachfront Land Re: Block 8A, Parcel 19 & 20 (Part), prepared by Charterland Ltd for DRCL, 5 November, 2012
[22] Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013
[23] Analysis of Proposed Roadway Changes Revision 3, prepared by Integra Realty Resources-Caribbean for DLS, 25 February, 2013
[24] Valuation: Crown Lands Re: Proposed Closing & Vesting of West Bay Road, prepared by Charterland Ltd for DRCL, 12 December, 2012

- Charterland adds a premium of CI$2,417,000 to its calculation to reflect the marriage value to the freeholder of the Soto Land (that is, CIG) when also taking control of the leasehold interest.

With regard to the land designated for the new road, DRCL has agreed, through the NRA Agreement, to transfer to CIG without compensation any land required for the ETH Extension or related works. As outlined in Section 4.2.5, DLS concludes that no overall compensation would have been due to DRCL in any event, as a result of the overall positive effect on DRCL lands of teh ETH Extension. Therefore, the value of these 65,000 square feet should be excluded from the valuation of the Soto Land leasehold.With regards to the marriage value, it must be recognized that no value has been attributed to any uplift in the existing public beach following the closure of the WBR and the creation of the Public Beach Park on the Soto Land. The public beach cannot likely be the site of any commercial development and therefore cannot increase in market value. However, there is likely to be an increase in the public beach's intangible value for citizens and tourists resulting from the removal of the WBR, improved facilities and green spaces and improved parking, etc. Whilst these benefits cannot be readily quantified they are real and should be recognized PwC therefore believes half of the marriage value calculated by Charterlands, that is CI$1,200,000 should be included in the valuation as a proxy for the enhanced social value of the public space.

The resulting value of CI$5.5m has an NPV value of $6.7m.

4.2.18. New Public Beach and Public Beach Park development costs

DRCL will carry out development of the New Public Beach and of the Public Beach Park, based on CIG's specifications, for an amount not to exceed $3m.

4.2.19. West Bay pedestrian and bicycle paths

DRCL will build pedestrian and bicycle paths for use by the public as set out in the Second Amendment. The paths will approximately follow the portion of the WBR which is to be closed as well as the ETH from Governor's Way to Batabano Road. Furthermore, as set out in the Third Amendment, DRCL undertakes that, in the area from the Public Beach Park to Raleigh Quay, the paths will be located west of all major structures and buildings and no more than 200 feet from the high water mark. Following their construction, DRCL will be responsible for their maintenance.

DRCL estimates the paths will be approximately 19,500 feet long and 12 feet wide and cost $4.42 per square foot based on a hot mix asphalt surface[25]. This represents a total construction cost of $1.0m.

Although the pedestrian and bicycle paths will be for public use in perpetuity, there will not be any registered rights or other type of servitude in respect of the paths. DRCL retains the right, at its discretion, to relocate or realign the paths located on its land. PwC understands DRCL requires this right to enable it to develop its lands according to its future requirements. Despite the lack of registered rights, PwC believes the cost incurred inlaying the paths should be recognized since DRCL's obligation to provide them is clearly set out in the Second Amendment.

However, PwC does not believe any benefit to CIG should be given for the value of the land beneath the pedestrian and bicycle paths for the following reasons:

- We understand from discussions with DRCL that the presence of the paths could be beneficial to the development potential of DRCL's West Bay lands. Accordingly, the resulting value uplift compensates DRCL for the use of its land for the paths; and
- DRCL will not provide title or other registered rights over the paths land to CIG.

4.2.20. Land and access road for Sunrise Adult Training Centre

DRCL will transfer to CIG three acres of land located west of the ETH near Camana Bay, the exact location to be agreed by DRCL and CIG. DRCL will ensure that two acres of the land are filled to four feet above mean sea

[25] Email from DRCL to PwC, 13 September, 2012

level and that the land will have road access. Although the Second Amendment states that the purpose of the land is for a new Sunrise Adult Training Centre, CIG will have the right to use the land for other purposes or sell it for commercial development should it chose to do so.

DLS estimates the land has a market value of CI$2.50 per square foot. When including the cost to fill two acres as required, this results in a market value of CI$585,000[26]. This is lower than an independent valuation prepared for DLS by Bould Consulting, which assessed the value at CI$795,000[27]. DLS believes that Bould Consulting's value is overestimated. Also, an independent valuation prepared for DRCL by Blue Point Consultants Ltd assessed the value at CI$523,000[28] when including the cost to fill two acres as required. PwC has therefore relied on the DLS and Blue Point valuations which have almost the same result and has used the average of the two.

Accordingly, the total value comes to CI$554,000.

Based on the proposed route of the access road and an estimated cost per liner foot to lay, the NRA has estimated a total cost of providing the road access to the Sunrise Adult Training Centre at CI$318,000[29]. DRCL is also responsible for subdividing the land, at a cost estimated by DLS of CI$10,000. However, DLS highlight that its land value estimate is based on the assumption of full access and planning subdivision and, given that the costs of road access and subdivision should be apportioned between the remaining DRCL land parcels in this subdivision, DLS do not consider that these additional costs of access and subdivision should be included in the estimate of benefit accruing to CIG.

Accordingly, the total value comes to CI$554,000 and has an NPV value of $0.7m.

4.2.21. Land for educational and community purposes and for a cemetery

DRCL will transfer to CIG 20 acres of land located within the West Bay Properties, west of the ETH and north of the Reverend Blackman Road extension, the exact location to be agreed by DRCL and CIG.

Although the Third Amendment states that 15 acres of the land is to be used for educational and community purposes whilst 5 acres are to be used for a new cemetery, CIG will have the right to use the land for other purposes or sell it for commercial development should it chose to do so.

DLS estimates the land has a market value of CI$1.35 per square foot, which results in a market value of CI$1,175,000[30] for the 20 acres. This is lower than an independent valuation prepared for DLS by JEC Property Consultants, which assessed the value at CI$1,742,000[31]. DLS believes that JEC Property Consultants' value is overestimated. However, an independent valuation prepared for DRCL by Charterland Ltd assessed the value at CI$1,740,000[32] while a second valuation prepared for DRCL by DDL Studio Ltd assessed the value of 37.32 acres at the West Bay site atCI$2,845,000[33], which is equal to CI$1,525,000 for 20 acres. PwC has therefore relied on the three independent valuations which have similar result and has used the average of the three. Accordingly, a value of CI$1,669,000 has been retained.

[26] Report on the For Cayman Investment Alliance (FCIA) Second Agreement, The Valuations & Estates Office, Lands and Survey Department 2 October, 2012
[27] Property Appraisal, Undeveloped land, part of existing parcel, Block 13C, Parcel 22, prepared by Bould Consulting Limited for DLS, 22 August, 2012
[28] Valuation of Land at Block 13C Parcel 22 (part), prepared by Blue Point Consultants Ltd for DRCL, 24 January, 2013
[29] Summary of Approximate Quantities and Preliminary Estimate, Driveway for new Sunrise Adult Training Centre , National Roads Authority, 17 September, 2012
[30] Report on the For Cayman Investment Alliance (FCIA) Second Agreement, The Valuations & Estates Office, Lands and Survey Department 2 October, 2012
[31] Valuation Report of Proposed Parcel at Block 4D Parcel 450, 293, 210 (Part), prepared by JEC Property Consultants Ltd for DLS, August 2012
[32] Valuation Report: Land Re: Proposed West Bay Community Park, prepared by Charterland Ltd for DRCL, 20 September, 2011
[33] Valuation Report of Land Parcels at Block & Parcels 4D106, 174, 210, 293 & 450, prepared by DDL Studio Ltd for DRCL, 13 October, 2011

The value of the land must also reflect the cost of subdividing the land (estimated by DLS at CI$15,000). The total value of the land is therefore CI$1,684,000.

The value of CI$1,684,000 has an NPV value of $2.1m.

4.2.22. Land at Smith's Cove

DRCL will transfer to CIG parcel 7C70 at Smith's Cove, an approximately 2.4 acre lot located along South Sound Road next to the Smith's Cove Public Beach.

DLS estimates the land has a market value of CI$23.84 per square foot, which results in a market value of CI$2,520,000[34]. This is lower than an independent valuation prepared for DLS by Blue Point Consultants Ltd, which assessed the value at CI$2,960,000[35]. DLS believes that Blue Point Consultant's value is overestimated. However, an independent valuation prepared for DRCL by Charterland Ltd assessed the value at CI$2,850,000[36]. PwC has therefore relied on the two independent valuations which have almost the same result and has used the average of the two.

Accordingly, the total value comes to CI$2,905,000 and has an NPV value of $3.5m.

4.2.23. ETH Expansion construction

Expansion of the ETH, that is transforming it from a two lane road to a four lane divided arterial road from the BOBR to the LSR, will be carried out by the NRA and DRCL.

The NRA is responsible for the work from the BOBR to the Lawrence Boulevard Roundabout ("LTBR1"). Its budgeted costs for this work, to be agreed in advance, will be paid by DRCL. DRCL is directly responsible for the work from the LTBR1 at its sole cost and expense.

NRA has prepared an estimate of its costs from BOBR to LTBR1 of CI$6.7m[37]. PwC's understands that this cost has not yet been agreed with DRCL as the budget for this work.

DRCL has prepared a high level estimate of its costs from LTBR1 to LSR of $1.7m to $2.0m[38], with a midpoint of $1.85m. PwC's understands that this cost has not yet been agreed with the NRA as the budget for this work.

Taken together, these amounts represent a total estimated cost for the ETH Expansion of $10.0m. As per clause 15 of the Third Amendment, any difference between the agreed cost of the ETH Expansion and $11m shall be applied to the NPV cap of $52.95m of the $53m Abatements. Accordingly, assuming the agreed cost for the ETH Expansion is $10.0m, the $53m Abatements will be adjusted to $51.95m.

[34] Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013
[35] Valuation of Land at Block 7C Parcel 70, prepared by Blue Point Consultants Ltd for DLS, 10 December, 2012
[36] Valuation: Development Site Re: Land on South Church Street; Block 7C Parcel 70, prepared by Charterland Ltd for DRCL, 16 July, 2012
[37] Email from NRA to PwC, 18 March, 2013
[38] Email from DRCL to PwC, 10 April, 2013

4.2.24. Summary of Infrastructure and SMB Hotel development financial analysis

A summary of the financial analysis of the infrastructure and SMB Hotel development component of the NRA Agreement is presented in **Figure 6**.

Figure 6
Summary of the financial analysis of the infrastructure and SMB Hotel development component of the NRA Agreement ($m)

	Benefits to CIG	CIG Costs / Divestments
1. ETH Extension construction	37.3	-
2. NRA monitoring of ETH Extension and New Barkers Road construction	-	0.8
3. New Barkers Road construction	1.2	-
4. Additional NRA operating costs of ETH Extension	-	5.9
5. Land required for ETH Extension provided by DRCL	-	-
6. WBR closure land vested to DRCL and subsequent DRCL land value uplift	-	55.4
7. Land required for ETH Extension purchased from third parties and paid for by DRCL	1.6	-
8. Old Barkers Road closure land vested to DRCL and subsequent DRCL land value uplift	-	1.7
9. Land required for New Barkers Road provided by DRCL	-	-
10. SMB Hotel development fees and import duties rebate	-	10.5
11. Value uplift of CIG lands subsequent to WBR closure	2.0	-
12. Import duties waiver for public infrastructure constructed by DRCL	-	-
13. Cash grant paid by DRCL to CIG	5.0	-
14. Existing and required public rights of way to the sea along WBR extinguished	-	2.9
15. Land for New Public Beach	4.0	-
16. Additional NRA operating costs of ETH Expansion	-	1.0
17. Leasehold interest in Soto Land	6.7	-
18. New Public Beach and Public Beach Park development costs	3.0	-
19. West Bay pedestrian and bicycle paths	1.0	-
20. Land and access road for Sunrise Adult Training Centre	0.7	-
21. Land for educational and community purposes	2.1	-
22. Land at Smith's Cove	3.5	-
23. ETH Expansion construction	10.0	-
Total	**$78.1**	**$78.2**

Note: Amounts rounded to nearest $0.0m

On the basis of the financial analysis described above, the exchange of benefits concerning road infrastructure, land and the construction of the SMB Hotel would appear to represent costs and value of divested assets to CIG

which are essentially equal to the financial benefits which CIG can expect to receive. If the replacement value of the road were used (as outlined in Section 4.2.6), rather than the uplift value approach, CIG would achieve a net benefit of $12.5m.

Moreover, the following considerations must also be taken into account:

- The most important contribution by CIG to the NRA Agreement is the divestment of the closed WBR and Barkers lands, valued at $55.4m representing a share of WBR and Barkers land value uplift for which CIG is foregoing a direct cash compensation. This value uplift, while real, is difficult to estimate and does not constitute an immediate source of cash for DRCL. Further, for DRCL to recoup the value of this uplift requires substantial additional investment in the construction and operation of a major hotel. This represents a relatively high risk venture in the current economic climate. While PwC believes it is appropriate to include this amount among the CIG costs and divestments under the NRA Agreement, it does not require any disbursement of funds by CIG.
- Most of the benefits CIG is to receive will materialize in the short term. DRCL has completed most of the work on the ETH Extension and has already paid CIG the entire $5m grant.
- The quantified benefits do not include intangible benefits such as the anticipated improvements to the existing public beach following the closure of the WBR and the creation of the Public Beach Park. However, the quantified costs do not include intangible costs either, such as the potential social impact of reduced beach access to the public along the length of the former West Bay Road.
- Finally, and perhaps most importantly, this financial analysis set out above does not take into account the economic benefits which CIG can expect from the NRA Agreement and which are analyzed in Section 5.

4.3. Stamp duty, development fees and import duty abatements and SMB Hotel Tax Rebate

The NRA Agreement provides DRCL with certain abatements up to an NPV amount of $52.95m (the "$53m Abatements"). This amount is to be adjusted for any difference between the agreed upon cost of the ETH Expansion and $11m. As set out in Section 4.2.23, the cost estimates for the ETH Expansion provided to PwC by the NRA and DRCL, respectively, indicate the NPV cap of the abatements will in fact be decreased to $51.95m. Although the cost of the ETH Expansion has not yet been agreed upon by the NRA and DRCL, PwC has used this $51.95m amount.

The $53m Abatements are calculated as the sum of the following, on an NPV basis:

- 100% abatement of development fees, including royalties and mitigation fees payable in respect of the award of a coastal works licence or a coastal works permit, on all properties of DRCL or its affiliates; PwC assumes this applies to all properties and developments of DRCL and its affiliates since no restrictions are specified
- 100% abatement of import duties payable by DRCL or its affiliates; PwC assumes this applies to all properties and developments of DRCL and its affiliates since no restrictions are specified;
- 100% abatement of stamp duties payable by DRCL or its affiliates pursuant to the Stamp Duty Law (2007 Revision) or the Land Holding Companies Share Transfer tax Law (2007 Revision) ; PwC assumes this applies to all properties and developments of DRCL and its affiliates since no restrictions are specified;
- 50% abatement of stamp duty payable in respect of all leases in DRCL's West Bay properties;
- 50% abatement of all taxes levied pursuant to the Tourist Accommodations (Taxation) Law for the SMB Hotel for a period of 10 years after its opening; and
- Based on a 10% discount rate; there is no time limit on the $53m Abatements, the effective limit being the attainment of the adjusted NPV value which is assumed to be $51.95m.

In order to be eligible for these incentives, development adjacent to the closed portion of the WBR must be predominantly hotel/tourist resort oriented, along with ancillary projects such as condominiums, associated real estate and other amenities.

The "value" of the $51.95m is subject to interpretation. Two factors must therefore be considered.

Firstly, because of the time required to negotiate the Second Amendment, the Third Amendment and other delays, it is reasonable to assume that many of the expenditures DRCL is expected to make as a result of the NRA Agreement, including expenditures subject to the abatements, will be made later than originally foreseen. In the original version of the NRA Agreement, the NVP cap of these abatements was $24m. CIG and DRCL presumably wanted these abatements to have a value of $24m at the start of the NRA Agreement. Under the Third Amendment, the NPV cap of these abatements was raised to $52.95m. However, since the $53m Abatements are calculated as an NPV value at December 2011 at a 10% discount rate, delaying expenditures increases the value of the abatement expressed in nominal dollars. Using a 10% discount rate, $53m in December 2011 is worth approximately $60m in April 2013.

Secondly, a lower discount rate would result in a higher NPV value while a higher discount would result in a lower NPV value. PwC was not able to obtain a clear understanding from CIG nor DRCL as to how the 10% rate was negotiated. It would appear to be a compromise between:

- CIG's cost of borrowing, which is approximately 5% to 6%; and
- DRCL's target equity rate of return for its development, which DRCL has indicated is significantly higher than 10%.

To place the $53m Abatements into perspective, PwC calculated the value of the abatements when applied to the DRCL Development Plan and the Hotel Tax Rebate for the SMB Hotel. This calculation is based on the following assumptions:

- The DRCL Development Plan is carried out by DRCL according to the start date and end date for each project as indicated in the plan; where a project takes more than one year, it is assumed that costs are incurred evenly over the construction period;
- Costs in the plan are in 2012 dollars; inflation is calculated using a 2% annual rate for amounts spent after 2012;
- Development fees are charged at a rate equivalent to $15,700 per room as calculated by DRCL;
- Import duties are charged at a rate equivalent to $23,000 per room as calculated by DRCL; and
- The Hotel Tax is 13%.

PwC did not calculate the following potential abatements:

- Stamp duty, since DRCL owns all of the land required for the DRCL Development Plan;
- Stamp Duties in respect of leases at West Bay properties, since DRCL did not provide information regarding current or future leases; and
- Royalties and mitigation fees payable in respect of the award of a coastal works licence or a coastal works permit, since DRCL did not provide information on any works which would cause such royalties or fees.

Based on the assumptions set out above, DRCL would benefit from the $53m Abatements until mid-2019, during which period it would forego paying approximately $81.3m in fees and Hotel Taxes to CIG when expressed in nominal dollars. This assumes that DRCL would try to benefit from the $53m Abatements as soon as possible. Since DRCL would reach the $51.95m cap in 2019, it would only benefit from the Hotel Tax Rebate for the SMB Hotel for between four and five years before reaching the total NPV cap.

Even after applying the $53m Abatements to the entire DRCL Development Plan, potential net incremental development fees and duties from the plan total approximately $39m on an NPV basis (using a 10% discount rate), which is equal to $162m on a nominal basis. This is in the context of a total development cost of $1.1bn on an NPV basis (or $1.9bn on a nominal basis) spent by DRCL from 2012 to 2039.

Arguably therefore, if the $53m Abatements were effective in incentivizing DRCL to carry out the DRCL Development Plan, this would deliver a positive incremental benefit to public finances over the medium to long term, even after allowing for the full $53m Abatements and before considering the wider economic benefits. However, in the absence of detailed DRCL Return on Investment ("ROI") projections it is not possible to gauge whether or not the $53m Abatements are actually necessary in order to make the DRCL Development Plan commercially viable.

Since the $53m Abatements are capped at $51.95m (on an NPV basis), the abatements would be sufficient to cover taxation on each of the following projects included in the DRCL Development Plan:

- WB Lands Condo 1 (100 units)
- WB Condos 2 (50 units)
- WB Hotel 2 (300 rooms)
- WB Hotel 3 (150 rooms)
- Eco-Tourism Hotel (100 rooms)
- Commercial Centre 1 (50,000 square feet)
- WB Condos 3 (100 units)
- Commercial Centre 2 (50,000 square feet)
- Housing development at Crymble Landholdings (partial)
- Housing development at CIYCAM Lands (partial)

According to the DRCL Development Plan, the first eight of these projects represent a total investment of approximately $415m (on a nominal basis) and are scheduled to be built between 2012 and 2017.

DRCL has not made any property development commitments under the NRA Agreement other than the reopening of the SMB Hotel. Accordingly, the eight projects set out above may not all be built by DRCL. Also, the NRA Agreement allows the $53m Abatements to be applied, for the most part, to any DRCL projects, excluding leases at its Camana Bay commercial properties. Accordingly, it is impossible to determine with any degree of certainty the actual projects which might directly result from the $53m Abatements, as opposed to those which would have been carried out in any event, absent the incentives.

The Third Amendment amends the definition of Development Fees to include mitigation fees, which are taken in this context to mean compensatory mitigation relating to development on environmentally sensitive lands and coastal works. Clause 47 of the Third Amendment also includes provisions dealing with the determination and payment of compensatory mitigation for coastal works. [CIG has confirmed to PwC that this clause will not inhibit the role of a future cabinet in assessing compensatory mitigation and or royalties from coastal works and/or development on environmentally sensitive land]**[to confirm based on final version]**. However, any mitigation fees will be subject to the $53m Abatements, which is not limited to a fixed time period or geography. Accordingly, in considering future DRCL applications for coastal works and development on environmentally sensitive lands, such as in the Barkers area, CIG will need to consider whether the proposed developments generate sufficient genuine economic benefits as well as their impact on the environment.

Part I of the Investment and Development Incentives Schedule of the Third Amendment, which sets out the $53m Abatements, also provides, "for illustrative purposes only", an explanation of the purpose of the $53m Abatements. In summary, $37m is for the "partial recovery of amounts expended by DRCL to construct various road works" and other funding provided by DRCL while $16m is "for development incentives to re-furbish the SMB Hotel".

This explanation was not included in the original NRA Agreement, in the Second Amendment or in the first versions of the Third Amendment. Moreover, it does not correspond to the rationale which has always been provided to us; that is, that the purpose of these abatements is to incentivise DRCL to develop the SMB Hotel and other hotel/tourist resort-oriented development. PwC understands that DRCL is providing CIG with public infrastructure and other tangible benefits in order to secure the closure of the WBR and, in the absence of the WBR closure, DRCL would not provide this public infrastructure or other tangible benefits.

Based on its understanding of the commercial substance of the transaction PwC believes the $53m Abatements must be considered in terms of their effectiveness as incentives to DRCL for economic development. If DRCL does not develop new hotels or resorts, it will not be able to claim these abatements. We therefore have not included any portion of the $53m Abatements in the analysis set out in Section 4.2.

4.4. Hotel Tax Rebate for other hotels and stamp duty rebate for Caymanian purchasers

The Hotel Tax Rebate is applicable to all hotels opened, reopened, renovated or refurbished by DRCL during the 30 years from 2013 to 2043. The rebate is applicable for a ten year period following the hotel opening or reopening following renovation. Accordingly, the Hotel Tax Rebate could potentially provide a tax rebate to DRCL until 2053.

The Hotel tax Rebate for the SMB Hotel is treated separately since it is included in the $53m Abatements.

Because the Hotel Tax Rebate can be applied to any DRCL hotel property built or acquired subsequent to the NRA Agreement which is opened or refurbished up to 2043, it is not possible to estimate CIG's foregone revenue.

PwC has calculated the potential cost of the Hotel Tax Rebate if applied to all hotels included in the DRCL Development Plan other than the SMB Hotel, for a period of ten years starting from their planned opening date.

DRCL has not advised of any plans to acquire existing hotels and, as such, the potential tax forgone on any future DRCL hotel acquisitions and subsequent renovations is not measurable.

The calculation is based on the current Hotel Tax rate of 13%. Should this rate change in the future, the potential cost of the Hotel tax Rebate could vary.

The results of these calculations are shown in **Figure 7**.

Figure 7
Potential Hotel Tax Rebate ($m in NPV at 3.5%)

	Rebate over 10 years
WB Hotel 2	$10.8
WB Hotel 3	4.0
WB Hotel 4	5.1
Eco-Tourism Hotel	3.9
Total	**$23.8**

When applied to all DRCL hotels included in the DRCL Development Plan other than the SMB Hotel, the 50% rebate provided by the Hotel Tax Rebate is estimated to represent $23.8m (on an NPV basis) of CIG foregone revenue. This is equivalent to $34.1m on a nominal basis. The potential value of the Hotel Tax rebate is subject to significant potential variance. It could be much lower if DRCL does not open all of the hotels included in the DRCL Development Plan, if these hotels have fewer rooms, if the hotels have a lower than expected occupancy rate or if the average rate charged per room is lower than expected. Conversely, the potential value could be much higher if DRCL builds bigger hotels, charges more per room or achieves a higher occupancy rate or if CIG were to increase the hotel tax. DRCL can also claim the Hotel Tax Rebate for any hotel it opens or renovates, including hotels it could build on properties outside of West Bay (for example at Camana Bay) or if it acquires an existing hotel and undertakes renovations.

The value of the Hotel tax Rebate must also take into account two other considerations: the need of the Hotel Tax Rebate to spur investment and the economic benefits of investments caused by the Hotel Tax Rebate.

PwC understands the goal of the Hotel Tax Rebate is to spur the development of new hotels or the renovation or refurbishment of existing hotels by DRCL. DRCL verbally represented to PwC that it would not likely undertake

hotel investment in the Cayman Islands as currently planned without the Hotel Tax Rebate. However, PwC has not been provided any analyses supporting this position and it is outside the scope of the Independent Review to establish the need for the Hotel Tax Rebate to make hotel investment financially feasible. Also, given the wide geographical scope and very long period during which the Hotel Tax Rebate is applicable, it is not possible for PwC to judge whether the Hotel Tax Rebate would have a significant impact on a hotel investment decision in the Cayman Islands nor what the likely impact on competitors' investment decisions would be.

To PwC's knowledge, a similar rebate on hotel taxes has never been made available by CIG to a developer. Although CIG has in the past negotiated other incentives with hotel developers on a case by case basis, there is clearly a risk that the Hotel Tax Rebate could set a new precedent in the Cayman Islands, which would weaken CIG's negotiating position with alternative potential hotel investors.

The economic benefits of the Hotel Tax Rebate are analyzed in Section 5.

The NRA Agreement also provides concessions for Caymanian purchasers of property in DRCL's Camana Bay and WBR properties (which include the areas covered by the DRCL Development Plan).

From a VfM and economic impact perspective, these concessions are expected to have limited impact and, arguably, they provide a general benefit for Caymanians, albeit only those with the resources to acquire higher-end property.

As such, and in light of the lack of any detailed information on the real estate components of the DRCL Development Plan, and likely Caymanian participation, PwC did not perform a separate quantification of the value of this tax rebate.

However, it is noted that such concessions, if applied solely to DRCL sales, could potentially distort the Cayman Islands real estate market to the disadvantage of competing property developers.

5. Assessment of economic and social benefits of the Agreement

5.1. Introduction

This Section of the report provides an assessment of the economic and social impacts to CIG and its citizens that could result from the NRA Agreement.

The expected outcomes from the NRA Agreement are the redevelopment of the SMB Hotel and other real estate developments focused on the tourism sector as set out in the DRCL Development Plan, road infrastructure improvements and $5m invested in Government programmes. The impacts that flow from these outcomes can be captured as follows:

- **Tourism**: redevelopment of the SMB Hotel and its promotion will impact on the Cayman tourism economy, the investment could also have impacts on the labour market and skills;
- **Road infrastructure**: investment in the road network could impact on transport efficiency, road safety, the environment (e.g. noise, local air quality, greenhouse gases, etc), accessibility and integration; and
- **Government programmes:** the proposed $5m investment in CIG programmes, together with DRCL's contribution of land for public beaches, the Sunrise Adult Training Centre and Educational and Community purposes, will have wider impacts relating to recreational facilities, housing, education etc, albeit PwC notes that CIG has not made any commitments in the NRA Agreement with respect to implementation of these programmes.

PwC has used economic impact analysis to estimate the scale of these impacts on the Cayman Islands' economy using two indicators to quantify economic activity: **economic output**, as measured by the Gross Value Added ("GVA"), and **employment** supported.

PwC's economic impact analysis was conducted in May 2012. Since that time, as a result of the delays in completion of the amendments to the NRA Agreement, DRCL's work on construction of the SMB Hotel and other developments has been correspondingly delayed. Furthermore, DRCL has now determined that the SMB Hotel shall be demolish and reconstructed, rather than the original renovation and extension approach.

For the purposes of this final report, PwC reconfirmed with DRCL in April 2013 that the construction cost and parameters of the SMB Hotel development and the wider DRCL Development Plan remain valid, albeit commencement and completion dates are all impacted by the delays in the completion of the amendments to the NRA Agreement.

This assessment is an integral part of the VfM assessment.

The Section is structured as follows:

- A description of the economic impact assessment framework;
- A summary of the analysis of the gross impacts that are expected to arise from the NRA Agreement;
- A summary of the assessment of the net impacts of the NRA Agreement;
- An assessment of the sensitivity of the results to key assumptions; and
- A summary of the key conclusions.

5.2. Economic impact assessment framework

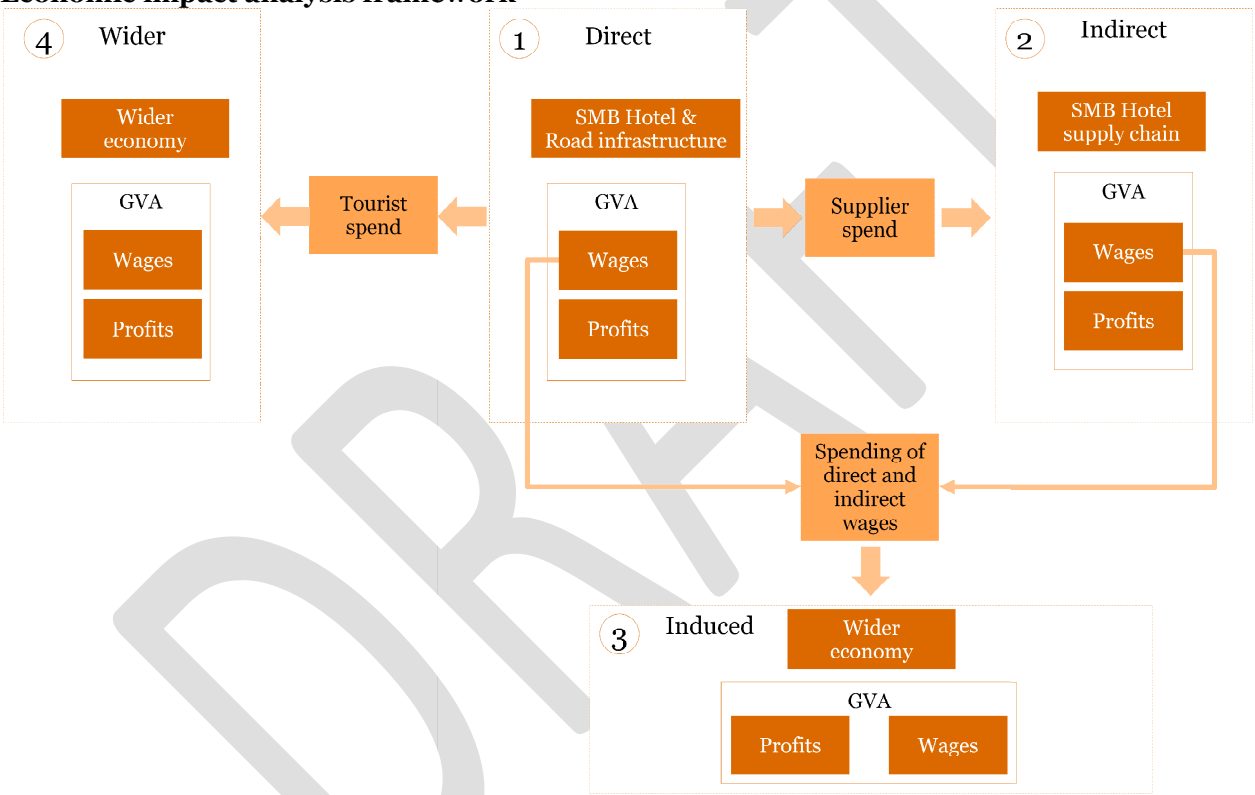
Economic impact analysis is an established methodology for assessing and valuing the economic impacts of investments. The technique is widely used by national governments, non-governmental organisations,

multinational companies and other stakeholders across a range of emerging and developed countries.[39] This part of the Section introduces this methodology as it has been applied it to evaluate the NRA Agreement's impact on the Cayman Islands economy.

PwC's approach has considered the impact of the NRA Agreement on two indicators of economic activity. The economic output as measured by GVA is estimated alongside the total number of jobs supported by the expected outcomes from the NRA Agreement. This provides an estimate of the 'gross' impact associated with the NRA Agreement. This gross impact is then adjusted to take account of the economic activity displaced from other parts of the Cayman Islands' economy (e.g. tourists that would have come to the Cayman Islands anyway). The incremental impact of the NRA Agreement is then estimated by deducting the economic activity that would have happened in a counterfactual scenario in which the NRA Agreement was not in place. This provides an estimate of the 'net' impact associated with the NRA Agreement. Importantly, this analysis assesses the impact on the Cayman Islands only and does not include the impact on other countries.

Figure 8

Economic impact analysis framework



The impact on GVA and jobs is divided into four types: direct, indirect, induced and wider impacts. Such a division reflects the large network of interdependencies between industries in an economy, and allows the capture of the full effect flowing from the NRA Agreement and its outcomes. **Figure 8** provides an overview of these impacts:

1. **Direct impact** corresponds to the contribution made to the Cayman economy as a direct result of the NRA Agreement. In PwC's base case scenario (Scenario 1) with the NRA Agreement, this refers to the wages, profits and jobs that are expected to result from the redevelopment and operation of the SMB Hotel by DRCL.
2. **Indirect impact** is created primarily by the purchase of goods and services from firms that are directly involved in SMB Hotel's redevelopment and operation. This supports profits and wages that accrue across the supply chain.
3. **Induced impact** is the additional impact on the economy resulting from increased expenditure by the workforce employed directly by DRCL and indirectly by its supply chain, as income earned by these

[39] See for example, HM Treasury (2011) 'The Green book – Appraisal and Evaluation in Central Government'

employees is spent on various goods and services, leading to further economic activity and employment in the Cayman Islands.

4. **Wider impact** captures economic activity resulting from the outcomes of the NRA Agreement that are not captured through the direct impact from the SMB Hotel and its supply chain. Wider impacts include expenditure in the Cayman economy by tourists staying at the SMB Hotel. Besides its impacts on tourism, the NRA Agreement could give rise to two other wider impacts:
   - The impact on the road infrastructure which arise from the closure of WBR and the extension of ETH: these impacts will potentially manifest themselves in terms of improved transport efficiency, accessibility and integration, enhanced road safety and the environment; and
   - The potential benefits of the investments in CIG programmes, including those related to housing and education, which are enabled by DRCL's cash grant to CIG of $5m together with DRCL's contribution of land for the Sunrise Adult Training Centre and Educational and Community purposes.

The assessment described so far provides an estimate of the 'gross' impact that could be expected to result from the NRA Agreement and its expected outcomes. Some of the activity captured in this analysis, however, will not be new or additional to economic activity that would have taken place on the Cayman Islands in the absence of the NRA Agreement. To establish how much of this impact is likely to be additional, the gross impact must be adjusted for displacement and then compared to a counter factual scenario.

Displacement effects take account of economic activity that has been shifted from another part of the Cayman Islands. For example, tourists staying at the SMB Hotel but who would have stayed at another hotel on Grand Cayman had the SMB Hotel not been developed.

To estimate the 'net' impact of the NRA Agreement, the economic outcomes must also be compared to a counterfactual scenario which assumes that the NRA Agreement was not put in place. Section 3 of this report provides further details of the counterfactual scenario**s** that PwC has considered in this report. They are summarized in **Figure 9**.

Figure 9

Summary of scenarios

	With the NRA Agreement	Without the NRA Agreement
SMB Hotel only	Scenario 1: DRCL develops SMB Hotel only	Scenario 1a: No development
SMB Hotel and DRCL Development Plan	Scenario 2: DRCL develops SMB Hotel and the additional developments set out in the DRCL Development Plan	Scenario 2a: SMB Hotel is not developed; some of the developments which form the DRCL Development Plan proceed including the eco-tourism hotel and half of the condominiums, but they are developed with a ten year lag on current plans

Source: PwC

Finally, standard practice in economic impact analysis is to convert the economic impacts that accrue over the lifetime of the investment into present values. To achieve this, a discount rate is used to convert the future flow of GVA to present values. The CIG proposes a discount rate of 3½%. The discount rate is a key assumption in the analysis. An alternative discount rate can be derived from the cost of capital – or the interest rate at which CIG can borrow – and reflects the cost to government of funding the NRA Agreement. At present the government yield on 10 year borrowing stands at approximately 5½%. The sensitivities of the analysis are considered later in this Section of the report.

5.3. Estimating the economic and social impacts 'with the NRA Agreement'

This part of the Section presents PwC's analysis and assessment of the economic and social impacts as the Cayman Islands 'with the NRA Agreement' and its expected outcomes. It describes each of the stages set out in **Figure 10** for this analysis in detail for **Scenario 1** in which DRCL develops only the SMB Hotel (and the

associated condominiums). In the description below, all references to the SMB Hotel also include these associated condominiums.

The Section also provides a summary of the analysis for **Scenario 2** in which DRCL develops the SMB Hotel and the additional developments set out in the DRCL Development Plan. The key assumptions that influence these estimates are set out in **Appendix 5**.

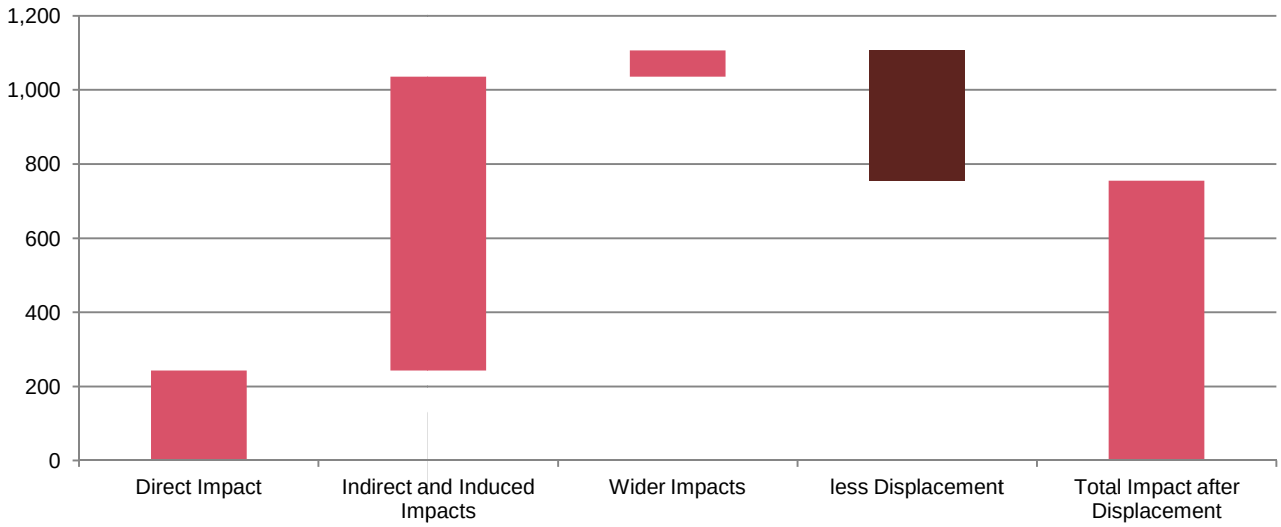
Figure 10

Overview of the stages in the economic impact assessment

PwC's analysis indicates that the economic impact of **Scenario 1**, which comprises the SMB Hotel's construction and operation, would be a $755 million contribution to Cayman Islands' GVA over the 22 year life time of the project. This in turn is estimated to support employment of 1,651 man years through the construction period and 890 FTEs during the operating period.

Figure 11

With NRA Agreement: Economic impacts of Scenario 1 (the SMB Hotel only) (Net present value of GVA, $m)

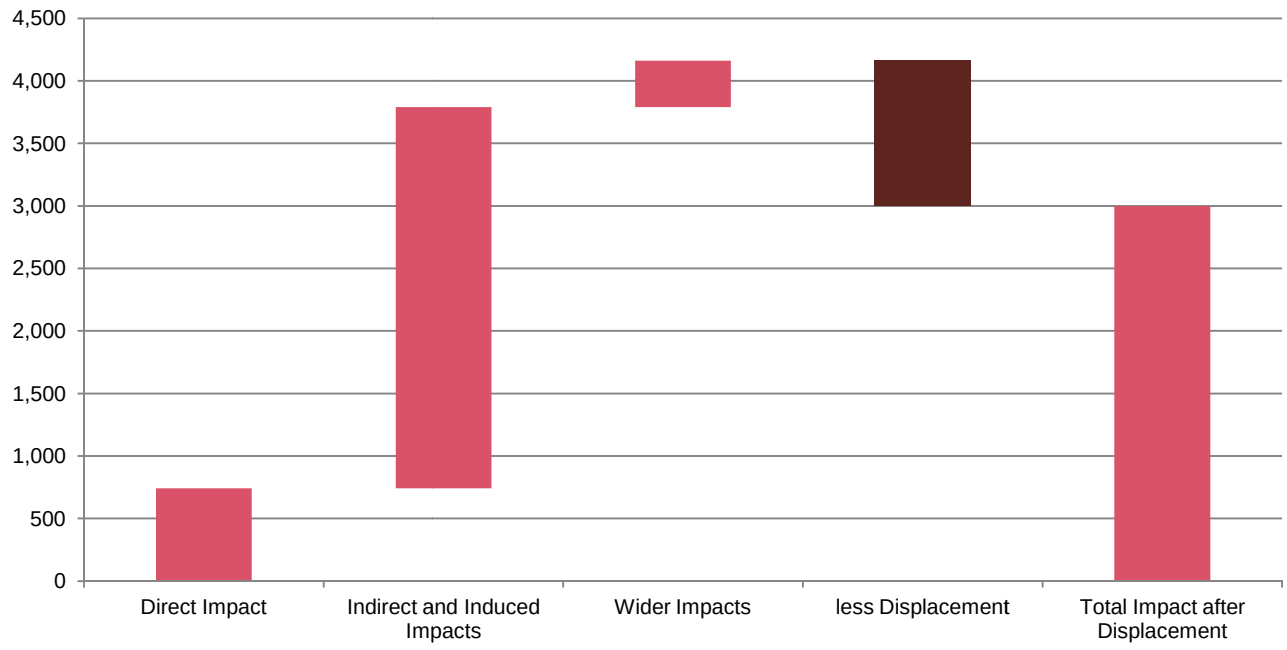


Source: PwC analysis

PwC's analysis indicates that the economic impact of **Scenario 2**, which also includes the DRCL Development Plan, would be a $2,999 million contribution to Cayman Islands' GVA over the life time of the project. This in turn is estimated to support employment of 11,957 man years through the construction period and 4,069 FTEs during the operating period. As these additional developments are assumed to take place in 10 years time the economic impact is assessed for 22 years from 2022.

Figure 12

With NRA Agreement: Economic impacts of Scenario 2 (the SMB Hotel and DRCL Development Plan)
(Net present value GVA, $m)



Source: PwC analysis

5.3.1. Measuring the direct economic impacts

PwC has estimated the direct economic impact, measured in terms of GVA, by estimating the net present value of its component parts ((a) operating profits[40] and (b) payroll) over the lifetime of the SMB Hotel. Based on assumptions provided by DRCL, the lifetime of the SMB Hotel project for the purpose of the economic impact analysis has been defined as 22 years, comprising two years of construction and 20 years of operation.

The operational period used broadly reflects the expected economic life of the SMB Hotel redevelopment. In this way, the costs and benefits of the development are "matched". For those other developments which form part of the DRCL Development Plan and where the construction period extends beyond that of the SMB Hotel, the analysis adopts an equivalent approach by assuming that the economic lifetime is 20 years from completion of construction before significant additional investment is required.

(a) Estimating operating profits

Operating profits, defined as revenues minus costs, over the lifetime of the SMB Hotel were estimated based on the revenue and cost assumptions provided by DRCL. Over the construction period, operating profit is negative as construction costs are borne and no revenues are realised. Over the operating period, operating profit is positive as recurrent revenues are higher than ongoing costs.

It has been assumed that revenues follow a three-year 'adjustment period' where occupancy is lowest in the first year of operation, climbs in the second year and reaches a stabilized (constant) level in the third year. This reflects an expectation of the period necessary for the marketing effort to take its full effect on visitor arrivals.

[40] Operating profit refers to the accounting concept of earnings before interest and tax (EBIT).

(b) Estimating payroll

The payroll estimate is based on assumptions provided by DRCL on payroll costs as a proportion of total operating costs during the operating period of the hotel.

(c) Estimating GVA

The GVA has been calculated in each period as the sum of (a) operating profits and (b) payroll.

According to the latest staffing plans, the major hotels in the Cayman Islands expect 71% of their staff in 2012 to be migrant labour[41]. Migrant employees tend to repatriate some of their income to their home country. Similarly, some of the operating profits are likely to flow outside the Cayman Islands. This creates a "leakage" from the Cayman Islands' economy and means that some of the economic impacts associated with the NRA Agreement are likely to flow outside the country.

To estimate the scale of the leakage it is necessary to understand the proportion of repatriated income. In the absence of locally collated data on repatriation, PwC has estimated a proxy by calculating the average remittance plus holiday spending abroad and divided this by the average wage of a Cayman worker. This estimate suggests that approximately 12% of earnings leaks out of the economy.

Similarly, consideration needs to be given to whether or not DRCL will reinvest any profits earned from its proposed developments in further developments in the Cayman Islands (rather than in other countries). Data are not available on which to base an assumption on the proportion of profits that will be reinvested in the Cayman Islands; PwC has, therefore, assumed that all profits are reinvested in the base case assumptions. The sensitivity analysis later in this Section of the report tests the significance of this assumption.

Appendix D sets out in more detail the assumptions that have been used to estimate the direct impacts.

5.3.2. Establishing the most appropriate multipliers

'Multipliers' are used to estimate the indirect and induced impacts that might be expected to result from the construction and operation of the SMB Hotel. Multipliers are a way of estimating how direct economic impacts cascade through an economy. Economic multipliers can refer to the ratios of the wider GVA impacts on the economy relative to the initial direct GVA impact (as measured above). They can also be expressed in terms of employment multipliers, determined by the ratios of jobs created in the wider economy relative to the direct employment impact of the firm or industry.

Multipliers vary across the sectors of the economy and across countries as they reflect the unique structure and inter-dependencies in the economy being analyzed. Multipliers are usually estimated using Input-Output (IO) tables or Social Accounting Matrices (SAMs). PwC has not been able to calculate multipliers for the Cayman Islands as the data required is not available. Instead, following an extensive review of the available international literature, the most appropriate multipliers have been identified. PwC has taken the multipliers from a study by Tian et al. of the economic impact of tourism in Hawaii. This has the benefit of being a relatively recent study, and Hawaii has some similar economic features to the Cayman Islands (e.g. in terms of being an island economy with comparable per capita income levels and a significant tourism sector). Multipliers for Jamaica or the Dominican Republic would be less relevant as their economies are larger and more diverse than the Cayman Islands, whereas more comparable Caribbean economies, such as Bermuda, do not produce these estimates. The match is necessarily imperfect and so the precise multipliers should be treated with some caution.

Figure 13 summarizes the multipliers used in this analysis.

[41] Source: Cayman Islands Department of Immigration – Statistics of Caymanians/non Caymanians employed in hotels under business staffing plan board for March and April 2012

Figure 13

Multipliers used to estimate the indirect and induced impacts

Type of multiplier	Multiplier	Impact
Construction multiplier	0.86	Additional benefits to the economy from the construction of the SMB Hotel
GVA multiplier	1.4	Additional benefits to the economy that accrue in the form of GVA to employers and employees from operation of the SMB hotel
Intermediate consumption multiplier (local)	1.4	Additional benefits to the economy from spending on locally produced intermediate inputs
Intermediate consumption multiplier (imports)	-0.197	Lost benefits to the economy from spending on foreign produced intermediate inputs

Source: Tian et al. (2011) The direct and indirect Contributions of Tourism to Regional GDP: Hawaii, the Economic Research Organisation at the University of Hawaii.

5.3.2.1. Construction multiplier

The construction spending by DRCL on the SMB Hotel complex will have a positive impact on the economy. Income that is received by firms in the hotel's supply chain will be spent on other goods and services or invested elsewhere in the economy. A construction multiplier measures the positive impact on Cayman's GVA from $1 of construction spending due to these inter-linkages.

Construction multipliers should be felt over a longer period than consumer spending multipliers since the initial expenditure has a positive impact on the capital stock of the economy.[42] For this analysis, it is assumed that the impact from the construction multiplier is spread over a four-year period after the initial investment is made.

5.3.2.2. GVA multiplier

The income generated from DRCL's development which accrues either to the firm(s) operating the SMB Hotel in the form of operating profits or to employees as payroll distributions also has a positive impact on the economy. Income that is accrued by the operating firm(s) can be used to invest in further developments or can be distributed to its investors. Investors use this income to buy other goods or services, or they may chose to repatriate a proportion of the profit to their home country. Employees use their wages to consume other goods and services or to invest.

PwC has used a GVA multiplier to measures this impact. To reflect the lag between the period when GVA accrues and the period when economic benefits are realised, it has also been assumed that the impact from the multiplier is spread over two years following the direct impact. The GVA multiplier generates an economic benefit in every period that GVA positive accrues.

5.3.2.3. Intermediate consumption multiplier for local materials

The expenditure that DRCL makes on local materials that are required for the SMB Hotel's operations also has a positive impact on the economy. This expenditure is calculated by estimating the share of operating costs that relate to local materials, which was informed by DRCL. Economic benefits are realised as income that is received by upstream firms in the supply chain which is then spent on other goods and services, invested or distributed to employees.

To reflect the likely lag between the period when the expenditure occurs and the period when the economic benefits are realised, it is assumed that the multiplier operates over two years after the initial expenditure is made. The intermediate consumption multiplier for local materials generates an economic benefit in every period in the operating phase of the SMB Hotel.

[42] See Hamilton, J (1994) 'Time Series Analysis'

5.3.2.4. Intermediate consumption multiplier for imported materials

In contrast, the Cayman Islands economy will lose income when money is spent abroad on imported materials as income is redirected from the Cayman economy to trade partners. Based on information provided by DRCL, the expenditure that leaks out of the Cayman Islands has been estimated based on the share of operating costs that relate to imported materials.

To reflect the likely lag between the period when the expenditure occurs and the period when the economic costs are realised, it is assumed that the multiplier operates over two years after the initial expenditure is made. The intermediate consumption multiplier for imported materials generates this economic cost in every period in the operating phase of the SMB Hotel.

5.3.3. Measuring the indirect and induced economic impacts

The next stage of PwC's approach combines the direct GVA and employment impacts estimate in stage 1 with the multipliers identified in stage 2. This provides estimates for the indirect and induced impacts.

The indirect impact on the Cayman Islands economy is that which results from the purchase of goods and services by firms directly involved in DRCL's supply chain. The induced impact is the additional impact on the economy resulting from increased expenditure in the Cayman Islands by the workforce employed directly by DRCL and indirectly by people employed in its supply chain. This is equal to summation of the discounted present values of the GVA impact from the construction multiplier, GVA multiplier and intermediate consumption multiplier.

5.3.4. Estimating the employment supported by the NRA Agreement

The economic impact assessment can be expressed in terms of the employment that would be supported by the expected outcomes from the NRA Agreement.

PwC has separated the direct employment impact between the construction and operating periods of the SMB Hotel. Since the employment created during the construction phase will be for a defined period of two years, the construction employment is estimated in terms of "man years". The operations employment is estimated in terms of Full-Time Equivalents ("FTE"s), where one FTE refers to one person working full time for the economic lifetime of the investment.

These estimates are based on data provided by DRCL. DRCL derived its employment estimates for the construction phase based on historical outturns which suggest that every 4.1 jobs are associated with every $1million invested.

For **Scenario 1**, the development of the SMB Hotel only, DRCL's development is estimated to support 1,651 man years in the construction phase and 890 FTE positions for the 20 year operational lifetime of the hotel. For **Scenario 2**, with additional developments, 11,957 man years in the construction phase and 4,069 FTE positions for the operational lifetime of the hotel and additional developments.

A standard method for estimating the employment that would be supported by the indirect, induced and wider impacts of the NRA Agreement is to use employment multipliers. This method works in a similar way to the multipliers applied to estimate GVA, described above. However, the data are not available for the Cayman Islands to calculate the relevant multipliers, so PwC has instead taken an estimate of GVA per employee from the Cayman Islands' national accounts and applied different sector weights to get the most appropriate estimate of GVA per employee, see **Figure 14**. These estimates are combined with the relevant output from the GVA impact estimate to provide an estimate of the number of employees required to support the given level of GVA.

Figure 14

GVA per employee (2009)

	GVA per employees	Description
Used for construction impact	$85,737	Average GVA per employee less FISIM
Used for GVA impact	$79,045	Average GVA per employee weighted by CPI consumption basket
Used for intermediate consumption (local) impact	$74,098	Average GVA per employee weighted by Hawaii input-output tables expenditures
Used for intermediate consumption (imported) impact	$74,619	Average GVA per employee weighted by Hawaii input-output tables expenditures
Used for tourism expenditure impact	$55,007	Average GVA per employee weighted by tourism expenditures from Jamaica 2012 Oxford Economics report

Source: Economic and Statistics Office, Cayman Islands
Note: Financial services indirectly measured (FISIM) has been removed from the estimate of economy wide GVA to account for the distorting effect of financial flows through the Cayman Islands' economy.

5.3.5. Measuring the wider economic and social impacts of the NRA Agreement

The NRA Agreement is expected to lead to wider economic impacts beyond those captured above:

- Those which result from any additional spending by visitors to the SMB Hotel (and other hotels) outside the hotel;
- Those arising from possible pull-through from the marketing of the SMB Hotel if it boosts the profile of the Cayman Islands and attracts additional visitors to the Islands (who do not stay at SMB Hotel);
- Those arising from investment to develop hospitality skills, especially in the Caymanian workforce;
- Those arising from development of the road infrastructure, including any impacts on the quality of life of Cayman Islands citizens; and
- The contribution DRCL will make to the funding of CIG programmes.

Each is considered in turn below.

5.3.5.1. Impact of additional spending by visitors to SMB Hotel

As well as making expenditures inside the SMB Hotel, visitors that are attracted to the SMB Hotel are likely to make expenditures on the goods and services outside the hotel. This generates economic benefits as income is received by firms which is then spent on other goods and services, invested or distributed to employees (which is eventually spent or invested).

To estimate this impact PwC has selected a tourism multiplier from the international literature. When examining tourism multipliers they often display very substantial international variations depending on the structure of the economy in which the tourism activity takes place or the spending patterns of the recipients of these expenditures. The size of the economy can also explain differences between the Caribbean countries listed in **Figure 15**. The larger and arguably more diversified economies such as Jamaica and the Dominican Republic show considerably higher multipliers when compared to small countries and economies such as the British Virgin Islands and the Cayman Islands, which indicates the linkages to other sectors are more developed in larger economies.

Figure 15

Tourism multipliers – selected countries

Country	Size of multiplier	Country	Size of multiplier
Cayman Islands	0.65	**Antigua**	0.88
Bermuda	1.03 - 1.09	**Jamaica**	1.23 - 1.27
Dominican Rep.	1.2	**Bahamas**	0.78-0.79

Source: Meyer (2006) Caribbean tourism, local sourcing and enterprise development: review of the literature, Centre for Cultural Change, Sheffield Hallam University

As with the application of the other multipliers, PwC has spread the impact over two years after the initial expenditure occurs to account for expenditure lags. The tourism demand multiplier generates this economic benefit in every period in the operating phase where there are visitors to the SMB Hotel.

5.3.5.2. Development of hospitality skills

One of the potential economic benefits claimed for the NRA Agreement is that it will contribute to the development of better skills across the workforce employed in the hospitality sector. This, in turn, is expected to bring the opportunity for workers to improve their prospective lifetime earnings as well as contributing to the sector becoming more competitive internationally.

DRCL's has advised that it is keen to see opportunities for (additional) Caymanian employment at the SMB Hotel and that it expects that its preferred operator of the SMB Hotel will be willing and able to hire Caymanians and provide them with training working at their other hotels elsewhere in the world in advance of the SMB Hotel opening. In this way, it is hoped that the SMB Hotel can gradually employ more and more Caymanians. As yet, the DRCL has not signed an operating agreement for the SMB Hotel and DRCL has no contractual provisions with its operator.

The extent to which DRCL's proposed approach to recruitment and training will bring economic benefits over and above those captured in the preceding analysis depends on the nature of the additional skills which employees gain and its impact on their earnings ability, including:

- The amount of the benefit of having a more skilled workforce that will be captured by the operator of the SMB Hotel (rather than other employers in the sector). PwC expects that the operator of the SMB Hotel is prepared to invest in developing the skills of its workforce mainly to enable it to compete effectively in the marketplace. To the extent that it is able to do so, and it continues to employ the people that it trains, the economic benefits will already be captured as part of the direct economic impacts of the NRA Agreement because the earnings of workers at the SMB Hotel are a key element of the gross value added expected to arise from the NRA Agreement. As such they are already captured in PwC's analysis.
- The extent to which the employees can be expected to move to work for another employer in the sector where they can make use of the skills they have gained. If any of the employees who gain new skills as a result of working at the SMB Hotel move to work elsewhere in the sector (or, indeed, in other sectors) where the skills would be valued, then it is possible that other employers will be able to derive some of the value of the additional skills. This will only happen if the skills acquired are relevant to the new employer, rather than being specific to a particular employer.
- Whether other employers in the sector operating in the Cayman Islands will recognize the value of the skills which employees have acquired. Linked to the above, if prospective new employers do not (or cannot) recognize the skills that have been acquired, then they will not reflect them in how much they are prepared to pay the employees, and this will mean that the value of the new skills is lost.

PwC has reviewed the limited available evidence which informs the potential wider economic benefits of the investment in skills. PwC believes that the scale of the potential benefits is likely to be small compared to the direct, indirect and induced economic impacts for the following reasons:

- Much of the value of the investment in training and skills development will be captured by the operator of the SMB Hotel. Indeed, it is in the operator's interest to ensure that it captures as much of the benefit as possible by retaining the workers who it trains.

- Even if workers leave the SMB, not all of them will choose (or be able) to use their skills to the wider benefit of the Cayman Islands economy because:
  - Some will leave the Cayman Islands, perhaps to return to their home country;
  - Some will move to work in other sectors where their skills are not valued, and some may retire; and
  - Not all of the skills acquired will be transferable.

5.3.5.3. Development of the road infrastructure

The NRA Agreement provides for DRCL to fund a series of changes to the road infrastructure including the closure of WBR and ETH Extension and the expansion of the ETH from a two to a four lane highway between BOBR Roundabout to the LSR Roundabout.

The impacts of these improvements will potentially manifest themselves in terms of:

- Improved transport efficiency, accessibility and integration;
- Enhanced road safety and improved tourism product through increased pedestrianisation of WBR; and
- The environment (e.g. noise, local air quality, greenhouse gases and amenity).

The ETH Extension has been identified as a priority project by the NRA for almost a decade. It is seen as necessary for enabling the country's future (economic) growth. Specifically, it is expected to improve access between West Bay and George Town and significantly reduce traffic congestion on key parts of the West Bay-George Town peninsula roads. It is also seen as reducing the transport system reliance on WBR which is heavily exposed to major storms and hurricanes.

Some indication of the potential impact of the road changes related to WBR and ETH comes from a report prepared by Orth-Rodgers for DECCO Ltd, a DRCL enterprise, in June 2011[43]. This report examined the potential implications of the road changes and associated real estate developments on the volume of traffic flows and levels of congestion at peak hours between 7 and 9 am in the morning and 4 and 6 pm in the evening.

This report was conducted prior to the provisions in the Third Amendment relating to the expansion of the ETH. It found that two-way peak hour traffic volumes on WBR just north of Raleigh Quay were approximately 1,830 and 1,600 per hour in the morning and evening respectively. It also noted that whilst traffic volumes provide an important measure of activity, they do not indicate how well existing capacity meets demand. Where capacity is insufficient, especially at road intersections, this can cause congestion. The report, therefore, provided an assessment of the level of service ("LOS") provided at key intersections by examining the average total delay during peak hours (see **Figure 16**). The analysis showed that existing levels of service on ETH were generally acceptable at LOS 'b' or better during both peak periods whilst on WBR service levels were generally LOS 'c' or better although some side streets were at or over capacity (LOS 'd' or 'e').

Figure 16

Levels of service and expected delay for unsignalized intersections and roundabouts

Level of service	Expected traffic delay	Average total delay (seconds/vehicle)
a	Little or no delay	≤10.0
b	Short traffic delays	10.1 to 15.0
c	Average traffic delays	15.1 to 25.0
d	Long traffic delays	25.1 to 35.0
e	Long traffic delays	35.1 to 50.0
f	Very long traffic delays	>50.0

[43] Orth-Rodgers & Associates Inc, Traffic Impact Assessment of Proposed Esterley Tibbetts Highway Extension in Grand Cayman, Cayman Islands, report prepared for DECCO Ltd, June 2011

The report also considered the implications of the proposed changes to the road infrastructure and the associated real estate developments taking account of the underlying growth in the volume of traffic through the area as a result of increases in population and employment.

The analysis assumed a background growth rate of 3% per annum with a further 20% increase in traffic following completion of further DRCL developments. These assumptions were considered to be conservative by the report's authors[44].

The report concluded that there would be sufficient road capacity to accommodate the changes in road traffic associated with redevelopment of the SMB Hotel, noting that the increase in traffic volume would not be significant compared to existing traffic volumes. Looking further ahead, and anticipating the effect of additional development and greater background growth in traffic, the report projected that a significant increase in the expected volume of traffic on ETH would result in all but one of the intersections operating at LOS 'd' or better. The exception was the westbound right turn at the intersection of WBR and Lime Tree Bay Avenue which is projected to operate with a delay of 39 seconds during the evening peak hour, only 4 seconds above the LOS 'd' threshold.

No formal cost-benefit analysis of the road improvements has been provided. Some indication of the scale of the effects can be gleaned by considering the potential time savings. This can be done by assuming that, on average, 1,750 drivers are delayed twice every day for about five minutes (30 seconds at each of six junctions). On this basis, the equivalent of about 25 working days are lost each working day across the population, although the majority of the time is likely to be non-working time.

In addition, the expansion of the remainder of the ETH from a two to four land highway is expected to deliver significant additional transport benefits and also address potential bottleneck concerns adjacent to Camana Bay, which had been raised by the NRA.

The road improvements are also expected to contribute to improved road safety, especially along WBR. Specifically, they are expected to enhance the pedestrian experience on WBR and create safe bike lanes for recreational use along the highway extension. The significance of these improvements can be seen by considering the incidence of road accidents on WBR (see **Figure 17**): historically, WBR has accounted for over 10% of road accidents in the Cayman Islands, and the number of accidents increased by nearly 200% between 2005 and 2009. During the same period, the incidence of accidents per 1,000 vehicles increased by over 160%.

Figure 17

Road accidents in the Cayman Islands

	2005	2006	2007	2008	2009
Accidents					
West Bay Road	61	158	152	224	165
Total	492	1,186	1,310	1,498	1,421
% in West Bay Road	12.4%	13.3%	11.6%	15.0%	11.6%
Accidents per 1,000 vehicles	15.6	35.4	38.5	41.9	41.0

Source: Royal Cayman Islands Police Department

The closure of WBR is seen by DRCL as improving the pedestrian experience in the tourism intensive area to the South but is also seen by some as potentially restricting Cayman Islands citizens' access to Seven Mile Beach and depriving road users of beach and sea views. Whilst such impacts on safety and amenity should not be ignored, it is difficult to put a monetary value on them or, indeed, to assess their scale.

[44] Orth-Rodgers & Associates Inc

The Second and Third Amendments of the NRA Agreement include a number of new provisions relating to public beach access, namely:

1. Public Beach Park

Under the Second Amendment, DRCL will surrender its leasehold over the 'Soto Land' to the CIG. The Soto Land is adjacent to the WBR opposite the existing Public Beach. Accordingly, following the closure of the West Bay Road, the surrender of the Soto Land will enable CIG to establish a larger, upgraded Public Beach Park to the South of the SMB parcels, which will itself provide an access point for the beach along the stretch of closed WBR. In addition, under the Second Amendment, DRCL must complete works for the Public Beach Park, to specifications agreed by the CIG, up to a total cost of $3m.

2. New Public Beach

The Third Amendment requires DRCL to provide lands comprised in Barkers, Block 8A, Parcel 19 and part of Parcel 20, for the purpose of creating a new public beach.

3. Smith's Cove

The Third Amendment also requires DRCL to transfer lands adjacent to the public beach at Smith's Cove, Block 7C, Parcel 70, to become public lands.

4. Pedestrian and Bicycle Path

Finally, the Second Amendment includes a commitment for DRCL to *"provide pedestrian and bicycle paths for use by the public in perpetuity on the Public Beach Lands and through [those] parts of its land West of the ETH."* The Third Amendment includes a further commitment that *"with respect to the area from and including the Public Beach Park to Raleigh Quay DRCL undertakes to locate all bicycle and pedestrian paths it provides on its land West of all major structures and no more than 200 feet from the mean high water mark"*.

As discussed further in Section 6, this commitment stops short of any registration of new public rights of way on DRCL land and the actual pedestrian and bicycle path routes remain subject to variation. However, based on the planned routes provided by DRCL, the proposed pedestrian and bicycle paths offer public access to the beach along the length of the closed West Bay Road, in addition to new inland routes.

In light of the above, the general public would appear to have enhanced beach parks and facilities as a result of the amended NRA Agreement. While unregistered, the new pedestrian and bicycle pathways would arguably also have an added safety benefit, given the absence of vehicular traffic. Albeit, PwC notes that these enhancements must also be viewed in the context of the Third Amendment's waiver and relocation of existing and future public rights of way that would usually have been required of DRCL under the Cayman Islands Development and Planning Regulations.

In addition, the expenditure during the two year construction process will provide some opportunities for local contractors involved in the construction activity and the Third Amendment includes provisions in which DRCL undertakes to use and give preference to local service providers and subcontractors wherever reasonably possible.

5.3.5.4. Contribution of funding and land for CIG programmes

The NRA Agreement also provides for DRCL to contribute a $5m cash grant to CIG towards the cost of programmes. PwC understands that this investment will be split equally between a residential mortgage arrears assistance programme which will be made available to qualified Caymanians and a programme of other community works focused on improving education, parks and housing.

As yet, the precise way in which the funding will be used and, more importantly, the expected outcomes of the projects which make up these programmes are not well defined. This means that it is difficult to assess the potential impacts quantitatively, let alone put a monetary value on them. Instead, for the purposes of this

report, PwC treats DRCL's investment of $5m as revenue accruing to CIG which can be offset against the revenue foregone as a result of other elements of the NRA Agreement.

In addition, the Second Amendment of the NRA Agreement provides for the contribution by DRCL of three acres of land for the Sunrise Adult Training Centre, fifteen acres of land for Educational and Community purposes and five acres of land for a new cemetery in West Bay.

Once again, at this stage the associated CIG project outcomes are not yet fully defined and as such it is difficult to assess the quantitative impacts. Accordingly, for the purposes of this report PwC estimates the impacts in terms of the market value of the land to be transferred, as set out in Section 4.

5.3.6. Measuring potential displacement in the hotel market

The positive impacts of the NRA Agreement which arise from the impact of the SMB Hotel (**Scenario 1**), and the DRCL Development Plan (**Scenario 2**), may be partly offset if they displace visitors to other hotels in the Cayman Islands. Such an effect can arise in two possible ways:

- If potential visitors who use the SMB Hotel switch from other hotels (and accommodation) in the Cayman Islands; and/or
- If any aspect of the Cayman Islands' air transport capacity constrains the number of visitors to the Cayman Islands.

These possibilities are considered in turn.

5.3.6.1. Analysis of the hotel market in the Cayman Islands

PwC has used qualitative and quantitative approaches to examine the potential extent of displacement that might be expected from DRCL's developments once they are operational.

First, PwC has undertaken a qualitative analysis of DRCL's SMB Hotel proposition against existing hotels in the Cayman market. The analysis draws heavily on the REVPAR Report. It considers three key related features of the hotel development that influence its distinctiveness:

- The competitive offering;
- The geographical location; and
- The operator's brand positioning.

The mechanism by which these factors influence displacement and the extent to which DRCL's SMB Hotel may result in such displacement are described in **Figure 18**.

Figure 18

Assessing the distinctiveness of the SMB Hotel

Feature of the SMB Hotel	Impact on displacement	Extent to which the SMB Hotel may result in displacement	
Competitive offering	The more differentiated the tourism product, the greater the potential for the SMB Hotel to draw in additional tourists as opposed to displacing existing ones.	◔	The recent study of the Cayman Islands tourism industry by REVPAR International suggests that the new SMB Hotel would be positioned as a "lifestyle hotel", traditionally smaller than full-service hotels with a greater focus on the consumer. The report suggests that this positioning will attract a new-type of visitor to the Cayman Islands and that thus will help avoid direct competition with brands in the "luxury" and "upper-upscale" market.

Feature of the SMB Hotel	Impact on displacement	Extent to which the SMB Hotel may result in displacement	
Geographical positioning	A hotel operator that opens up in a new geographical location will be more likely to draw in new tourists as opposed to displacing existing tourists.	◑	SMB is one of the most popular locations for hotel developments in the Cayman Islands due to the good condition of the beach. The REVPAR Report, however, suggests that the hotel's position on this stretch of beach may be more favourable than other sections. It is argued that the positioning of SMB will appeal more to luxury-seeking tourists as it is one of the only sections that offers full sun exposure during the day and does not wash away.
Brand positioning and marketing reach of the operator	The brand positioning of the hotel operator will influence the type of traveller will be attracted to the hotel. A strong international brand may diversify the type and home location of traveller that is attracted.	◑	The hotel operator has yet to be identified but the RevPar Report suggests they would be "confident that they would reinforce Tourism office's image and quality goals". It is also likely that the hotel operator has primarily a US-market focus. This may be less successful in drawing in additional tourists from other geographies apart from North America. The hotel operator will have $2.5-3.5m annual sales and marketing expenditure to attract new customers. To put this in perspective, the Cayman Islands' tourism office's latest annual marketing budget was $12m.

Source: PwC analysis, REVPAR, DRCL Impact Assessment

Expected level of displacement: ● Very high ◕ High ◑ Medium ◔ Low ○ Very low

This qualitative analysis suggests that there are several reasons why the SMB Hotel might be expected to fill a gap in the market. On the other hand, the proximity of other hotels along SMB and the US-market focus of the likely operator heighten the risk of some displacement of visitors to other hotels in the Cayman Islands.

Second, two possible approaches can be used to derive quantitative estimates of the extent of displacement that might be expected over the operating life of the SMB Hotel:

- Analysis of how customers in different market segments might be expected to respond to the SMB Hotel's arrival on the market; and
- Analysis of the impact of historical hotel additions on tourist arrivals.

The first approach involves identifying the different segments of the tourist market in the Cayman Islands and analyzing the likely response to a new hotel market arrival within each group. The Cayman Islands tourist industry can be grouped into three distinct market segments: leisure, group and commercial. The REVPAR Report showed that the biggest group was leisure tourists.

Although there has been no primary research to test customers' potential response to the redevelopment of the SMB Hotel, existing evidence suggests that customers in each market segment are likely to respond in different ways to a new hotel:

- **Leisure**. The "hotel product" is one of several important factors when leisure travellers decide their holiday destination. Some travellers will make their decision to visit the Cayman Islands based solely on the availability of a particular hotel and others will decide on the Cayman Islands as a destination and then make their choice of hotel. It is the latter group that is most likely to give rise to displacement from existing hotels in the Cayman Islands whereas those travellers who decide to travel to the Cayman Islands only as a result of the new hotel are unlikely to provoke a direct displacement effect. In the absence of any empirical evidence, this analysis is based on the assumption that 75% of independent leisure visitors will be "additional" visitors and 25% will directly displace visitors to other hotels.
- **Group**. The "group" sector includes those visitors who travel to the Cayman Islands as part of a group for a conference, or as a prize from a sales event. For this market segment, a hotel's amenities and its branding are likely to be a significant factor when group travellers decide their destination. In the absence of any empirical evidence, this analysis also assumes that 75% of group leisure visitors will be "additional" visitors and 25% will directly displace visitors to other hotels.
- **Commercial**. The commercial (or business) segment of the market covers those travellers to the Cayman Islands who undertake the journey for business reasons, rather than consideration of the hotel product on

offer. In the absence of any empirical evidence, this analysis assumes that only 10% of business travellers to the Cayman Islands who are expected to stay at the SMB Hotel are "additional" visitors.

This framework has been used to estimate the proportion of visitors attracted to the SMB Hotel that are additional, rather than displacing others. The estimate of the extent of displacement is shown in **Figure 19** below.

Figure 19

Estimated displacement resulting from the SMB Hotel

Market segment	Estimated proportion of visitors derived from market segment in a stabilized year (REVPAR)	% displaced from existing hotels
Leisure	55%	25%
Group	28%	25%
Commercial	17%	90%
Total		**36%**

Source: PwC analysis

Overall, based on this approach, PwC assumes that 36% of the visitors to the SMB Hotel would otherwise have stayed at other hotels.

The second approach to estimating potential displacement is to use the experience of previous hotel market additions to estimate the extent of the additionality or displacement the hotel might be expected to generate. One such major addition to the hotel sector was the opening of the Ritz-Carlton in February 2006. As the first branded luxury full-service hotel on Grand Cayman, the REVPAR Report cites the opening of the Ritz-Carlton as being a major factor behind rising hotel occupancy in the Cayman Islands, which now "dominates the [luxury hotel] market"[45].

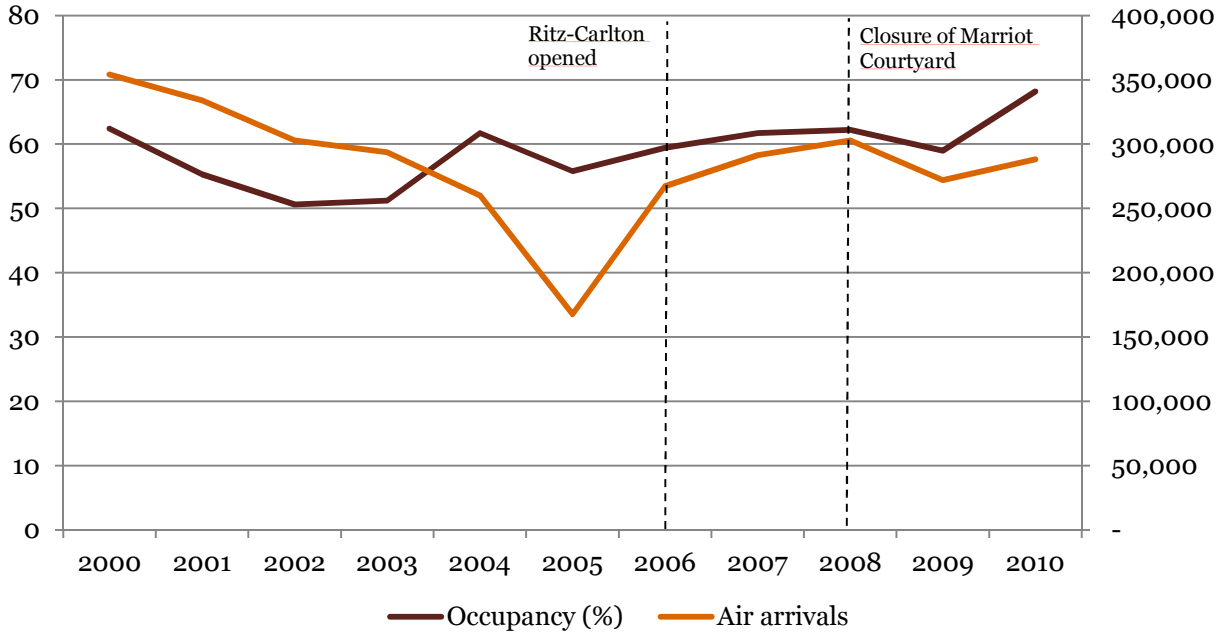
Using the available information relating to hotel occupancy, visitor arrivals by air and hotel visitor numbers, it is possible to evaluate the impact of the Ritz Carlton on the tourist market. Specifically, the approach compares the actual number of visitor air arrivals from the time that the Ritz opened to an estimated number of visitors if the Ritz-Carlton had not been developed. The difference between the two reflects the extent of displacement arising from the opening of the Ritz-Carlton.

Figure 20 shows that occupancy and visitor numbers increased gradually between the opening of the Ritz-Carlton in February 2006 and 2008.

[45] RevPar: "Re: Lodging Market Review Grand Cayman, Cayman Islands – Component 1"

Figure 20

Occupancy and visitor numbers before and after opening of Ritz-Carlton hotel



Source: Cayman Islands' Department of Tourism, PwC analysis

In estimating the number of air arrivals to the Cayman Islands without the Ritz-Carlton, it is important to recognize the impact of other potential demand and supply factors in any given year. On the demand side, a change in air arrivals may be influenced by the rate of economic growth in key arrivals markets (which influences arrivals in the leisure and group segments especially), growth in the offshore finance market (which influences arrivals in the business segment) and specific events which may draw visitors to the Cayman Islands in the leisure segment. On the supply side, air arrivals may be influenced by other hotel developments in the Cayman Islands, new air passenger routes opening access into the Cayman Islands and the impact of natural disasters or extreme weather conditions. The approach used takes account of each of these factors to estimate the number of arrivals by air in the Cayman Islands if the Ritz-Carlton had not been developed.

This is based on the following underlying assumptions:

- **Economic growth of key consumer markets**: it is assumed that the number of arrivals by air grows naturally at the same rate as real US economic growth throughout the period;
- **Bounce-back due to Hurricane Ivan**: it is assumed that arrivals in 2006 bounced back to a trend level following the adverse impact of Hurricane Ivan in 2004; and
- **Offshore finance market**: to some extent the effect of growth (or decline) in the offshore finance market is captured by accounting for real US economic growth between 2005-2007 but a further adjustment is made to business travel to reflect the contraction of financial services by 5% in the Cayman Islands in 2008[46] as a result of the financial crisis.

The results of applying this methodology are presented in **Figure 21** below.

[46] Source: ESO National Income Statistics, 2010

Figure 21

Estimation of the number of visitors to the Cayman Islands without the Ritz Carlton

	Actual number of arrivals by air	Change in arrivals by air	Effect of bounce-back from Hurricane Ivan	Effect of real economic growth in the US	Effect of offshore finance market growth	Estimated number of arrivals by air without the Ritz-Carlton
2004	259,929	-	-	-	-	-
2005	167,800	-	-	-	-	-
2006	267,258	99,458	62,385	4,460	-	234,645
2007	291,503	24,245	-	5,077	-	272,336
2008	302,879	11,376	-	-875	-4,955	285,673

Source: ESO, PwC analysis

The Ritz-Carlton was the only significant hotel addition in the Cayman Islands between 2006 and 2008 and is assumed to be the main supply side factor acting over this period. On this basis, the difference between the actual number of arrivals by air and the expected number of arrivals without the Ritz-Carlton presented in Figure 21 is the number of arrivals by air attracted to the Cayman Islands by the opening of the Ritz-Carlton. This is estimated in Figure 22 below. The analysis is limited to the period between 2006 and 2008 due to the large number of net hotel additions recorded in 2009 (which makes it difficult to isolate the impact of the Ritz-Carlton)[47].

The actual number of visitors to the Ritz-Carlton has also been estimated for this period using market occupancy data presented by REVPAR[48]. On this basis, the opening of the Ritz-Carlton resulted in a large number of additional visitors to the Cayman Islands when the hotel was first opened in 2006 but in 2007 and 2008, it is estimates that around a third of visitors to the Ritz were displaced from other hotels.

This stabilized result broadly corroborates with PwC's analysis of the behavioural impact in different market segments after a new hotel addition. Overall, it is suggested that 36% is a reasonable estimate for the amount of displacement likely from the SMB hotel addition in the Cayman Islands.

Figure 22

Estimation of the number of visitors attracted by the Ritz-Carlton

	Actual number of arrivals by air	Estimated number of arrivals by air without the Ritz-Carlton	Estimated number of visitors attracted by the Ritz	Estimated number of visitors who stayed in the Ritz	Estimated number of visitors displaced	% displacement
2004	259,929	-				
2005	167,800	-				
2006	267,258	234,645	32,613	26,823	-5,791[49]	-22%
2007	291,503	272,336	19,167	26,277	7,109	27%
2008	302,879	285,673	17,206	27,622	10,416	38%

Source: ESO, PwC analysis

[47] Department of Tourism, Cayman Islands
[48] RevPar: "Re: Lodging Market Review Grand Cayman, Cayman Islands – Component 1"
[49] Negative displacement implies that the Ritz-Carlton drew in visitors to the Cayman Islands who would not have previously stayed there in its first year of operation.

5.3.6.2. Analysis of infrastructure capacity of the Cayman Islands

Airport and airline constraints can limit the potential growth in tourists to the Cayman Islands. A constraint on visitor growth will limit the potential impacts from the expect outcomes expected from the NRA Agreement. Specifically, the visitors that are attracted to the re-developed SMB Hotel may displace visitors from other hotels on the Cayman Islands if the there is not enough capacity for all the visitors.

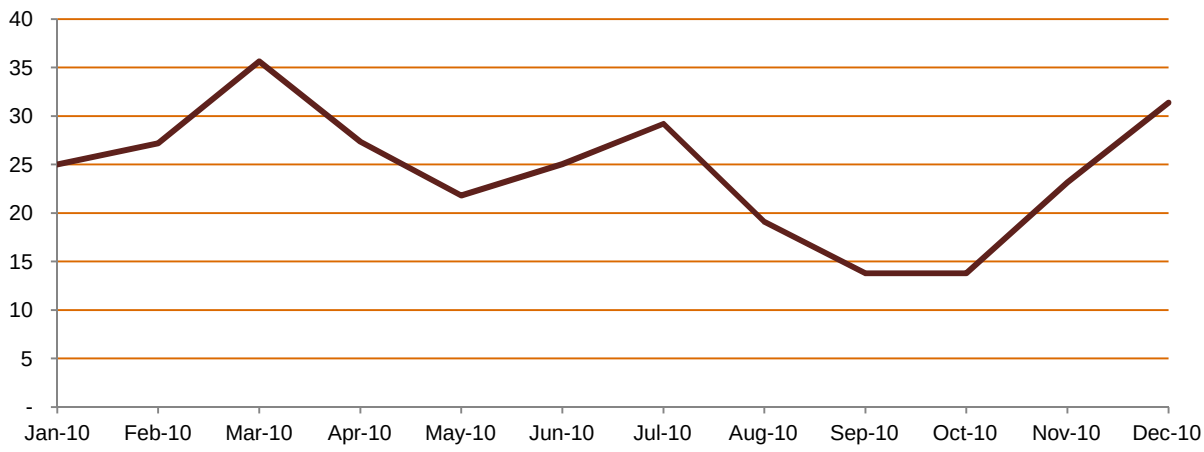
The capacity constraints can result from a number of sources:

- Airport – possibly from runway capacity, runway length, and terminal capacity; and
- Airlines – flight schedules and aircraft type determine the number of seats available for each destination.

According to the REVPAR Report, the Owen Roberts International Airport, the principal airport of entry for visitors to the Cayman Islands, offers a "good airlift compared to other Islands of a similar size". Annual data show that arrivals peaked in 1998 at 404,200 arrivals, and have since been on a downward trend reaching 288,272 arrivals in 2010, which indicates some spare capacity at the airport on an annual basis. Monthly arrivals data from 2010 show that arrivals peak at around 35,000 in March and fall to a low of under 15,000 in September. January, February and April have between 7,000 and 10,000 fewer visitor arrivals than March, this also suggests spare capacity at the airport if there is visitor demand to visit Cayman in these months. The REVPAR Report notes that capacity has been increased between 2009 and 2010, during that period 44,000 airline seats to the Cayman Islands were added, mainly from the US and Canada. A limiting factor, however, is a lack of direct flights from Europe to Cayman, which is partly due to the short runway. Plans to redevelop the airport have been delayed on environmental and cost grounds.

Figure 23

Visitor air arrivals to Cayman Islands, 2010 ('000s)



Source: Department of Tourism

5.3.7. Economic impact of SMB Hotel and DRCL Development Plan

PwC's analysis of the economic impact of **Scenario 2**, which includes re-development of the SMB Hotel and the DRCL Development Plan, follows the same stages described for **Scenario 1**. The analysis is based on data and assumptions that have been provided by DRCL (see **Appendix 5**). The key features of the analysis are as follows:

- The focus is on estimating the impact on GVA and jobs created.
- Revenues from the condominiums are expected to build up at the same rate as those for the SMB Hotel.
- The costs of operating the additional condominium developments are assumed to be based on the same assumptions as those used to estimate the costs of operating the condominiums which form part of the SMB Hotel redevelopment.
- The analysis uses the same multipliers to estimate the indirect, induced and wider impacts.

- The analysis applies the same displacement analysis to the DRCL Development Plan: in practice, the additional hotels will need to tap into a wider international market perhaps by targeting different market segments which means that the scale of displacement may be different from that for the SMB Hotel.

As there is less information on the revenue and cost assumptions for the housing and retail/office development, the potential impact has been excluded from this analysis. The sensitivity analysis later in this Section of the report tests this assumption.

5.3.8. Impact results

This part of the Section brings together the outputs from the economic impact analysis. The outputs from the assessment of **Scenario** 1 (the SMB Hotel Development only) and **Scenario 2** (the SMB Hotel Development and DRCL Development Plan) are set out in **Figures 24** and **25** respectively. This separates out the direct, indirect, induced and wider impacts that could result from the expected outcomes of the NRA Agreement. It presents the total impact over the lifetime of the project in terms of net present value (i.e. after applying the discount rate).

The gross impact of the SMB Hotel over the lifetime of the project is equivalent to $1,106m. The major component of this impact is through the indirect effect felt by firms and employees in the SMB Hotel's supply chain and the induced impacts this generates. The direct economic impact of the Hotel contributes about one quarter of its total impact due to these multiplier effects.

Some of the gross economic impacts are offset by the displacement of visitors from existing Cayman hotels. Using PwC's displacement assumption, the economic impact falls to $755m – around three quarters of the overall gross impact.

Overall, under Scenario 1, the developments are estimated to generate 1,651 man years employment during the construction phase and a further 890 FTEs during the operating period.

Figure 24
With NRA Agreement: Economic impacts of Scenario 1 (SMB Hotel only)

	Net present value to GVA ($m)	Impact in terms of employment	
		Construction (Man years)	Operations (FTEs)
(a) Direct impacts	$243m	743	570
(b) Indirect and induced impacts	$793m	907	680
(c) Wider impacts	$70m	-	95
Gross impacts (a) + (b) + (c)	**$1,106m**	**1,651**	**1,344**
less Displacement	$351m	-	454
Economic impacts	**$755m**	**1,651**	**890**

Source: PwC analysis
Note figures may not sum due to rounding

In **Scenario 2** (i.e. the SMB Hotel and DRCL Development Plan), PwC has examined the economic impact from the construction of nine hotel and condominium developments over a twelve-year period worth $643m at today's prices. The outputs from this assessment are set out in **Figure 25**. These developments involve over six times the construction expenditure proposed at the SMB Hotel. The direct impact of these developments is approximately three times that of the SMB Hotel, with the indirect, induced and wider impacts around four times as large. There are a number of reasons for this:

- Many of the investments occur several periods in the future, eroding the present value of the expected benefits; and
- Several of the hotel and condominium developments are expected to warrant a lower average daily rate than those developed at the SMB Hotel.

Figure 25

With NRA Agreement: Economic impacts of Scenario 2 (SMB Hotel and DRCL Development Plan)

	Net present value to GVA ($m)	Impact in terms of employment	
		Construction (Man years)	Operations (FTEs)
(a) Direct impacts	$743m	5,452	2,920
(b) Indirect and induced impacts	$3,047m	6,505	2,709
(c) Wider impacts	$371m	-	577
Gross impacts (a) + (b) + (c)	**$4,161**	**11,957**	**6,206**
less Displacement	$1,162m	-	2,137
Economic impacts	**$2,999m**	**11,957**	**4,069**

Source: PwC analysis
Note: figures may not sum due to rounding

5.4. Estimating the economic and social impacts 'without the NRA Agreement'

Up to this point, the economic impact analysis has considered the impact of the NRA Agreement focusing on the redevelopment and operation of the SMB Hotel, the expected implications of the road infrastructure improvements and the real estate developments planned by DRCL. The analysis has provided estimates of both the expected impact in terms of additional GVA and jobs.

In order to understand the incremental effect of the NRA Agreement, it is important to consider the expected pattern of development if there is no NRA Agreement and what economic and social impacts any developments might be expected to generate. Only by comparing this assessment with the expected impacts 'with the NRA Agreement' is it possible to understand the additional economic and social value provided by the NRA Agreement.

5.4.1. 'Without NRA Agreement' development scenarios

This part of the Section provides an assessment of the net economic and social impacts of the NRA Agreement. It starts by recalling the conclusions in Section 3 where PwC set out two alternative scenarios which describe what might happen 'without the NRA Agreement' (i.e. the so-called counterfactual scenario). These are as follows:

- **Scenario 1a** assumes that DRCL would not undertake redevelopment of the SMB Hotel nor would it undertake any of the other development included in the DRCL Development Plan for the period covered by the appraisal.
- **Scenario 2a** assumes that DRCL would undertake some of the projects in its Development Plan at some point in the future once the CIG is able and willing to fund the ETH Extension. Specifically, it assumes that the CIG would be in a position to finance the ETH Extension from public finances within ten years, and that DRCL would develop:
  - A 100 room eco-tourism hotel ten years later that currently planned (i.e. commencing in 2026);
  - About half of the condominium developments envisaged in the plan (i.e. 200 units), but again with a delay of ten years; and

– Housing (just over 1,000 units) and office/retail development (100,000 sq ft), again with a delay of ten years for both.

It also assumes that in the absence of the NRA Agreement neither DRCL nor any other developer would undertake alternative hotel developments that would not have been viable had the NRA Agreement and its associated development been carried out.

This part of the report analyses the potential economic and social consequences of each of the two scenarios described. The analysis relies on a similar approach for estimating the economic and social impacts as the 'with NRA Agreement' described above. As before, the analysis uses data and assumptions provided by DRCL as its starting point.

5.4.1.1. Scenario 1a

Scenario 1a envisages that DRCL will not redevelop the SMB Hotel without the NRA Agreement. This is because the NRA Agreement is essential to securing closure of WBR and without closure of WBR, it is most unlikely that redevelopment of the SMB Hotel will be feasible and viable, even if ETH is extended at some point in the future by CIG. On this basis, no developments will be undertaken either by DRCL or by any other developer.

The implication of this is that no adjustment needs to be made to the **Scenario 1** (assessed above) in order to derive the net impact of the NRA Agreement.

5.4.1.2. Scenario 2a

Scenario 2a envisages that DRCL will undertake some additional developments in the absence of the NRA Agreement, although it will not redevelop the SMB Hotel. The analysis is based on data and assumptions that have been provided by DRCL (see **Figure 26**). In the case of both the housing development and retail/office development, less information has been provided than for the hotels and condominiums.

Otherwise, the approach is as consistent as it can be with the approach used to estimate the economic and social impacts of the NRA Agreement:

- The focus is on estimating the impact on GVA and jobs created.
- Revenues from the condominiums are expected to build up at the same rate as those for the SMB Hotel.
- The costs of operating the additional condominium developments are assumed to be based on the same assumptions as those used to estimate the costs of operating the condominiums which form part of the SMB Hotel redevelopment.
- The analysis uses the same multipliers to estimate the indirect, induced and wider impacts.
- The analysis applies the same displacement analysis to the DRCL Development Plan: in practice, the additional hotels will need to tap into a wider international market perhaps by targeting different market segments which means that the scale of displacement may be different from that for the SMB Hotel.

Figure 26

Key data and assumptions underpinning Scenario 2a

	Construction	Scale	Development cost (US$m)	Revenues
Eco-tourism hotel	2026-2027	100 rooms	22.5	$350 per room per night; 65% occupancy
Three condominium developments	2023-2029	250 units	228.8	$0.8-1.2m per unit
Housing	2024-2049	1,009 units	974.8	$0.9-1.1m per unit
Office/retail development	2025-2030	100,000 sq ft	47.0	$45 per sq ft rent

The results from this analysis are summarized in **Figure 27**. The direct impacts from this **Scenario 2a** show a small positive impact ($117m). The indirect and induced impacts have a more substantial positive impact, which along with the wider impacts mean that the scenario generates a positive impact after displacement of $552m in net present value terms.

Figure 27

Without NRA Agreement: Economic impacts of Scenario 2a (limited DRCL Development Plan)

	Net present value to GVA ($m)	Impact in terms of employment	
		Construction (Man years)	Operations (FTEs)
(a) Direct impacts	$116m	1,609	600
(b) Indirect and induced impacts	$537m	1,984	591
(c) Wider impacts	$36m	-	77
Gross impacts (a) + (b) + (c)	**$690m**	**3,593**	**1,268**
less Displacement	$138m	-	369
Economic impacts	**$552m**	**3,593**	**899**

Source: PwC analysis

5.4.2. Net impact of the NRA Agreement

The final step in this analysis is to establish the net (incremental) impact of the NRA Agreement by comparing the GVA and job impacts estimated in the two scenarios *with the NRA Agreement* (**Scenarios 1** and **2**) and the two corresponding counterfactual scenarios *without NRA Agreement (***Scenarios 1a** and **2a**). This analysis is performed separately for scenarios focused on the SMB Hotel only (**Scenarios 1** and **1a**) and scenarios which also include additional developments from the DRCL Development Plan (**Scenarios 2** and **2a**).

The results are presented in **Figures 28** and **29** below.

Figure 28 compares the two scenarios which focus on the SMB Hotel redevelopment. It shows that the incremental benefits of the NRA Agreement are estimated to be an increase in GVA of $755m when expressed in net present value terms over the lifetime of the investment (20 years post construction). Expressed in terms of employment effects, 1,651 man years of construction are estimated to arise and 890 FTEs during the operational phase.

This is also equal to the expected benefits of Scenario 1 in which the impact of the SMB redevelopment is estimated. This is because the counterfactual scenario (i.e. without the NRA Agreement) assumes that none of the development would occur because the SMB Hotel would be unlikely to be viable without closure of WBR.

Figure 28

Net impact of NRA Agreement - SMB Hotel only

	Net present value to GVA ($m)	Impact in terms of employment	
		Construction (Man years)	Operations (FTEs)
(a) With NRA Agreement – Scenario 1	$755m	1,651	890
(b) Without NRA Agreement – Scenario 1a	$0m	0	0
Net impact (a) - (b)	$755m	1,651	890

Source: PwC analysis

Figure 29 compares the two scenarios which include both the SMB Hotel redevelopment **and** the DRCL Development Plan. It shows that the incremental benefits of the NRA Agreement are estimated to be an increase in GVA of $2,448m when expressed in net present value terms over the lifetime of the investment (20 years post construction). The net effects on employment are estimated to be 8,364 man years of construction and 3,170 FTEs during the operational phase. This is after offsetting the expected benefits from the limited developments assumed to be undertaken on a deferred basis without the NRA Agreement.

Figure 29

Net impact of NRA Agreement - SMB Hotel and DRCL Development Plan

	Net present value to GVA ($m)	Impact in terms of employment	
		Construction (Man years)	Operations (FTEs)
(a) With NRA Agreement – **Scenario 2**	$2,999m	11,957	4,069
(b) Without NRA Agreement – **Scenario 2a**	$552m	3,593	899
Net impact (a) - (b)	**$2,447m**	**8,364**	**3,170**

Source: PwC analysis

5.5. Sensitivity analysis

The penultimate part of the Section presents the sensitivity of the results of the quantitative analysis to the key assumptions that underpin them.

Figure 30 summarizes the six key sensitivities that have been tested as part of the sensitivity analysis. The table shows the assumptions that have been used in the base case, the sensitivities that have been tested and the reasons why the sensitivities were felt to be appropriate.

Figure 30

Summary of key sensitivities

Sensitivity	Base case assumption	Sensitivity tested	Reason for sensitivity analysis
Occupancy level and average daily rate	70% occupancy and ADR of $400 for the hotel	62% occupancy and ADR of $318 for the hotel[50]	DRCL has assumed that the SMB hotel will achieve a stabilized occupancy rate of 70% and a projected Average Daily Rate of $400. Together, these assumptions imply a RevPar of $280 for the hotel development. Both of these assumptions would imply a higher room revenue than has been achieved historically in the Cayman Islands. As a sensitivity, therefore, consideration is given to a scenario where occupancy and daily rates for the SMB Hotel achieve the same level as the Cayman Islands average over the last three years. The REVPAR Report shows that occupancy averaged 62% and average daily rate averaged $318 for full-service resort hotels over the last three years.
Extent of repatriation of earnings	12%	40%	For reasons of data availability, the base case assumption relies upon data for workers across the economy as a whole rather than those employed in the hotel sector. Given the nature of employment in the hotel sector, and the economic importance to the non-Caymanian workers of being able to remit earnings to their home country, actual remittance of earnings by workers employed in the hotel sector may be significantly understated. As a consequence, leakages are likely to be higher than in the base case.
Extent of reinvestment of profits	0%	10%	The base case assumption is that all profits derived from DRCL's developments are reinvested in the Cayman Islands. It is, however, possible that some of the profits derived from DRCL's developments will be invested outside the Cayman Islands at some point in time. The analysis tests the sensitivity of the impacts if 10% of DRCL's profits are invested outside the Cayman Islands.
Extent of displacement	36%	40%	No primary research has been undertaken to estimate the potential scale of displacement of visitors who would otherwise visit the Cayman Islands. The base case assumption is that 36% of visitors to the SMB Hotel displace other visitors to the Cayman Islands. As a sensitivity, consideration is given to the implications if displacement is confined to business visitors where there is less evidence that visitors are sensitivity to the hotels available.
Inclusion of housing and office/retail development	Excluded	Value added during construction and profit from sale/letting of space included.	DRCL has been able to provide detailed projections only for its proposed hotel and condominium developments; only limited information has been made available for the housing and office/retail developments. Consequently, they have not been included in the main analysis. As sensitivity, therefore, an estimate has been made of the value added which is expected to arise from the construction of the housing and office/retail developments. This comprises the value added in the local supply chain during construction plus the profit which DRCL expects to earn from the housing and office/retail developments. This is based on a comparison of the development costs with expected sales price.
Discount rate	3½%	5½%	The analysis has been based on a discount rate 3½% which is taken to reflect the social rate of time preference (and is referenced in the FFR). As a sensitivity, consideration has been given to the effect of using a discount rate which reflects CIG's current cost of capital. This is taken to be 5½%.

Source: PwC analysis

[50] Both the occupancy rate and RevPar assumptions have been kept stable for condominiums and other hotel developments in DRLT's Development plan.

Figure 31 summarizes the results of the sensitivity analysis. The top row of the table presents the expected NPV of the stream of GVA associated with each of the scenarios that have been analyzed. The second and third columns show the results for the two scenarios examined 'with the NRA Agreement (**Scenario 1** and **1a**) and the fourth and fifth columns show the results for the two scenarios examined 'without the NRA Agreement' (**Scenario 2** and **2a**). The two net impact columns show the net incremental impact of the NRA Agreement under the two sets of scenarios.

Each subsequent row shows the **change** in the expected NPV as a result of the sensitivity. The key points to note are that:

- The revenue expected to be earned at the SMB Hotel – which reflects the room rate and level of occupancy – has an important bearing on the estimated, additional GVA. Reducing the occupancy rate from 70% to 62% and reducing the ADR from $400 per night to $318 night in the SMB Hotel only leads to a reduction in the expected GVA of $152m. This is the same in both sets of scenarios because no adjustment is made to the expected revenues from the other hotels in the DRCL Development Plan.
- The extent to which some of the profits earned from the developments are repatriated has only a limited effect on the estimated benefits expressed in terms of additional GVA. This is because – as previously noted- the expected level of profits envisaged for the developments is relatively modest.
- The sensitivity analysis has also considered the significance of the proportion of earnings of those employed in the developments that are expected to be remitted to employees' home countries (or, indeed, anywhere outside the Cayman Islands). Increasing the proportion of earnings remitted from 12% to 40% reduces the net present value of the additional GVA by over $100m with only the SMB Hotel and by over $330m if DRCL's Development Plan is factored into the analysis.
- How far DRCL's developments displace visitors who would otherwise visit the Cayman Islands also affects the expected additional GVA. Increasing the level of displacement from 36% to 40% reduces the estimated increase in GVA by $50m (when only the SMB Hotel is considered) and by $146m (if both the SMB Hotel and DRCL's Development Plan are considered).
- The inclusion of the housing and office/retail development in the DRCL Development Plan increases the impact on GVA by just under 25% with the NRA Agreement (Scenario 2). Proportionately, it has a much bigger impact on GVA without the NRA Agreement (Scenario 2a). The estimated net impact is an increase in GVA of $212m which comes from the boost to the construction sector, the profits which DRCL expects to earn and the related indirect and induced effects. No consideration is given to any potential economic impact rising from the activities which occupy the office/retail development. In practice, this likely to be captured elsewhere in the analysis and displacement is a significant risk.
- The choice of discount rate has a significant effect on the net impact, especially under Scenarios 2 and 2a (with the SMB Hotel and the DRCL Development Plan). This is because many of the additional developments are expected to occur many years from now.

Figure 31

Impact of key sensitivities on expected GVA ($m, NPV)

Sensitivity	SMB Hotel only			SMB Hotel & DRCL Development Plan		
	With NRA Agreement (Scenario 1)	Without NRA Agreement (Scenario 1a)	Net impact	With NRA Agreement (Scenario 2)	Without NRA Agreement (Scenario 2a)	Net impact
Base case	$755m	$0m	**$755m**	$2,999m	$552m	**$2,448m**
Occupancy level and average daily rate	-$152m	$0	**-$152m**	-$152m	$0	**-$152m**
Extent of repatriation of earnings	-$103m	$0	**-$103m**	-$332m	-$44m	**-$288m**
Extent of repatriation of	-$22m	$0	**-$22m**	-$117m	-$32m	**-$84m**

Sensitivity	SMB Hotel only			SMB Hotel & DRCL Development Plan		
	With NRA Agreement (Scenario 1)	Without NRA Agreement (Scenario 1a)	Net impact	With NRA Agreement (Scenario 2)	Without NRA Agreement (Scenario 2a)	Net impact
profits						
Extent of displacement	-$50m	$0	**-$50m**	-$166m	-$20m	**-$146m**
Discount rate	-$127m	$0	**-$127m**	-$631m	-$174m	**-$457m**
Inclusion of housing and office/retail development	**$0**	$0	**$0**	+$726m	+$514m	**+$212m**

Source: PwC analysis

5.6. Conclusions

This Section has estimated the expected economic and social impacts of the NRA Agreement. It has focused on the potential implications of the redevelopment of the SMB Hotel and other real estate developments focused on the tourism sector as set out in the DRCL Development Plan and the associated road infrastructure improvements.

The scale of the expected impacts on the Cayman Islands economy has used two indicators: economic output, as measured by GVA, and employment.

The analysis is based on information and projections provided by DRCL and publically available sources, notably CIG statistics.

The incremental 'net' impact of the NRA Agreement has been estimated by comparing the economic activity that is expected to arise under two different scenarios with the NRA Agreement (one where development is limited to the SMB Hotel only and another which includes additional developments from the DRCL Development Plan) with the activity that would be expected in a counterfactual scenario without the NRA Agreement.

If the analysis is limited to the SMB Hotel only, the incremental benefits of the NRA Agreement are estimated to be an increase in GVA of $755m when expressed in net present value terms over the lifetime of the investment (20 years post construction). Expressed in terms of employment effects, 1,651 man years of construction are estimated to arise and 890 FTEs during the operational phase.

If the analysis includes both the SMB Hotel redevelopment and the DRCL Development Plan, the incremental benefits of the NRA Agreement are estimated to be an increase in GVA of $2,448m and the net effects on employment are estimated to be 8,364 man years of construction and 3,170 FTEs during the operational phase.

Analysis of the sensitivity of the impact estimates to the underlying assumptions shows that the key factors are:

- The revenue expected to be earned at the hotels, (which reflects the room rate and level of occupancy): reducing the room rate and occupancy rate at the SMB Hotel to the historic average across the Cayman Islands reduces the expected GVA by $152m.
- The proportion of non-Caymanian employees' earnings that are expected to be remitted to their home countries.
- How much of the housing and office/retail development envisaged in the DRCL Development Plan takes place.

In addition, the analysis has highlighted other potential wider economic impacts which are not captured in the quantitative estimates:

- The road improvements will contribute to alleviating congestion and improving road safety, although they may detract from amenity if they reduce beach access.

- Further hotel developments will boost the investment in developing the skills of workers in the tourism sector, although much of this benefit will be captured in the quantitative estimates.
- The promotion of new hotels will also help to boost the Cayman Islands as a tourist destination.

6. Risks related to the NRA Agreement

The NRA Agreement and the undertakings it includes contain a number of risks which could affect CIG. Some of these are quantifiable, essentially risks related to the road construction which must be carried out by DRCL. Other risks are real but not reasonably quantifiable and relate to the wider impacts or possible outcomes of the NRA Agreement such as the use of West Bay property, the use of tax abatements and the displacement of tourist demand from existing hotels.

6.1. Quantifiable risks

DRCL must construct the ETH Extension and the ETH Expansion between LTBR1 and LSR at its sole cost and expense according to the specifications set out in the NRA Agreement. Building a road necessarily presents risks which, if they materialize, will cause the actual cost of construction to be greater than the budgeted costs. DRCL must also fund the construction of the ETH Expansion between BOBR and LTBR1 up to a cost to be agreed upon with the NRA.

Without the NRA Agreement, the NRA would likely eventually build the ETH Extension and the ETH Expansion between LTBR1 and LSR itself, at some point in the future. Therefore, by assigning responsibility to construct the ETH Extension and the ETH Expansion between LTBR1 and LSR to DRCL, CIG gains a tangible benefit since any related cost overruns must be borne by DRCL. The NRA is responsible for any costs overruns related to the construction of the ETH Expansion between BOBR and LTBR1. However, for the reasons outlined below, PwC does not believe that the similar risks relating to construction of the New Barkers Road represent a true benefit to CIG.

The New Barkers Road will be built mainly in response to DRCL's needs and it is not certain that the NRA would build it in the future were the NRA Agreement not implemented. Therefore, even though DRCL proposes to assume all cost overrun risks relating to the New Barkers Road, this risk transfer is not considered a benefit to CIG and is not included in this analysis.

PwC identified and quantified a number of risks relating to construction of the ETH Extension based on discussions with the NRA and JEC. Risks are quantified based on the ETH Extension construction costs estimated by JEC and described in Section 4.1.1. Quantified risks also take into account the contingencies contained in the JEC cost estimates in order to avoid a double counting of costs. Finally, risk quantification is based on the state of design and construction as at 20 April, 2012 and takes into account the information communicated to JEC up to that date.

Construction of the ETH Extension appears to be relatively simple in nature and involves no major structures, aside from the culverts and possible bridges required for access to DRCL land parcels. These additional works are excluded from both JEC's cost estimate and the risk analysis on the basis that the works are not driven by public infrastructure needs but are instead required for private development purposes. The main risks identified with respect to the ETH Extension construction relate to the ground conditions, unexpected variations in input unit prices, unexpected design changes, variations in estimated quantities based on incomplete design, as well as some outlier events, such as a sudden price increase following a hurricane. The detailed treatment of these risks is set out below.

Construction of the ETH Expansion presents a lower level of risks than for the ETH Extension mainly due to the fact that it utilizes an existing road corridor with a well-known ground conditions. According to the NRA, some preliminary work for the new lanes was carried out when the current lanes were built. As a result, the ground settlement should be finished. In addition, potential cost over-runs that could arise from the design uncertainties at the planning stage are also significantly mitigated by the current geometry of the existing ETH. Residual risks are quantified for the potential variations in unit prices and for the cost over-runs related to the utilities relocation. The risks are allocated pro-rate between DRCL (18.5% calculated as the DRCL portion of $1.85m of the overall estimate of $10.0m) and CIG (remaining 81.5%).

6.1.1. Civil structure-related risks

DRCL plans to include an overpass as part of the ETH Extension in order to allow for better access between its properties on both sides of the ETH. However, the NRA informed JEC that it would not include such a structure if it were to build the ETH Extension itself, given that they are driven by private development, rather than public infrastructure, needs. Accordingly, JEC's cost estimate and the risk analysis excludes the impact of these additional works. Since there are no other significant civil structures included in the ETH Extension, no related risks are quantified.

6.1.2. Risks related to the ground conditions

JEC understands that the excavation and filling activities are completed for Phase 1A of the ETH Extension at the date of the first version of this report (circa 20-25% of the overall construction program). According to JEC, Phase 1A likely comprises the worse ground conditions of the entire ETH Extension, notably because of the low elevation, high water table and unsuitable soil quality. The remaining sections of the ETH Extension (Phases 1B and 2) are expected to have better ground conditions. However, to be prudent, JEC based its cost estimate for excavation and filling activities in Phases 1B and 2 on the actual costs incurred by DRCL for Phase 1A. Therefore, PwC does not believe there is a significant risk of cost overruns relating to ground conditions for these remaining phases.

As for the ETH Expansion, ground conditions of this existing corridor are well known in terms of settlement, and NRA is confident that the compaction works are estimated with a high degree of certainty. Main ground risk relates to the relocation of public utilities. Risk-adjusted value is estimated at 3% of the $10.0m ETH Expansion cost, i.e., $0.3m, of which $55,000 are allocated to the DRCL and $245,000 are allocated to the NRA.

6.1.3. Design-related risks

Design of the ETH Extension is approximately 90% complete at the time of the first version of this report. There remains the possibility of unexpected design-related events such as design changes during the remaining design work, design corrections related to the errors and omissions (including during construction phase) or variations in quantities during the remaining design period. Notwithstanding the absence of major civil structures and the advanced state of design, PwC believes it is prudent to provide for residual design-related risks. This risk is estimated at 3% of the ETH Extension project costs of $37.3m or $1.1m.

Considering that the ETH Expansion is utilizing the existing ETH corridor with a limited room for realignment or other future design changes, there are no residual design risks calculated for the ETH Expansion.

6.1.4. Construction risks related to unit prices and quantities

Unit price risks relates to the risk of unit prices for labour or materials being higher than budgeted. The ETH Extension costs estimated by JEC are based on current market prices in the Cayman Islands at the time of the first version of this report. Construction of the ETH Extension should be completed in 12 to 18 months and no major development projects, other than DRCL's, are expected during that period. Because of this lack of competing construction projects, therefore there appears to be limited supply side risk of ETH Extension unit prices increasing significantly. The exception to this is for materials whose price is linked to the price of oil. This risk is treated separately.

Quantity risk relates to the risk of actual quantities being greater than budgeted. Given the advanced state of the ETH Extension's design and the knowledge gathered from construction of Phase 1A, PwC does not believe this risk is significant. Considering the advancement of the design, the estimate of the quantities is likely to be relatively precise and warrant a correspondingly lower provision for potential future variations of the quantities.

To be prudent, PwC has calculated a risk related to quantities and unit prices equal to 5% of the ETH Extension project costs of $37.3m or $1.9m.

When considered on a joint basis, provisions for basic design and construction risks represent 8% of the project costs. This is a mid-point of the range of 5% to 15% generally recognized by the Quebec Association of Engineers for the level of design Class B (that broadly corresponds to where the current construction design stands, i.e., one notch below the complete final design allowing to proceed for construction bids).

As for the ETH Expansion, considering a generally low level of uncertainty of widening an existing roadway, the risk related to quantities and unit prices is estimated at 2% of the project costs, i.e., $0.2m of which 18.5% are allocated to DRCL and 81.5% to the NRA.

6.1.5. Risks related to the price of oil

The cost of asphalt, which is a major component, is closely related to the price of oil. To estimate this risk, the differential between the current spot oil price at the time of the first version of this report and the price peak of the last five years was calculated (+40%). This is then applied to the cost of asphalt included in JEC's ETH Extension cost estimate ($1.8m). However, there is no certainty that oil prices will reach this peak during the next 12 to 18 months. PwC has therefore applied a probability factor of 10%.

Based on these assumptions, the monetary value of this risk for the ETH Extension is $0.2m. This risk is not considered material for the ETH Expansion.

6.1.6. Hurricane related risks

As a result of its location, the Cayman Islands are exposed to high hurricane risk, which is exacerbated by the low elevation of the islands. In extreme cases, such as Hurricane Ivan, the infrastructure and property reconstruction and repair efforts can result in significant increases in prices for labour and materials during the repair period. This is particularly the case due to the finite labour market and shipping capacity. Based on discussions with JEC, it is possible that material and labour prices could increase by 20% following a major hurricane.

Assuming a major hurricane is a 1-in-50 years event (2% probability of occurrence) and assuming that it occurs when ETH Extension construction is half complete (therefore $18.5m of work remaining), the risk adjusted cost of such a hurricane is estimated at $0.1m.

6.1.7. Total quantified risks

The sum of the quantified risks discussed above for the ETH Extension is $3.3m. Since these risks are assumed by DRCL whereas they would have been assumed by the NRA without the NRA Agreement, they should be considered a benefit to CIG.

PwC identified one risk related to the ETH Extension which belongs to the NRA and which therefore should be considered a CIG cost. This is the risk of increased NRA operating and maintenance costs due to poor design or construction of the ETH Extension.

The NRA does not have as much control over the ETH Extension project as it would if it were responsible for its construction. There is therefore a risk for the NRA that operating and maintenance costs of the ETH Extension could be higher than expected because of poor design or construction resulting, for example, in the need to repave the road sooner than would normally be the case. This risk is not considered material in the case of the ETH Expansion since the NRA is directly responsible for most of the construction work.

For the purpose of this risk analysis, PwC has considered the cost of an unscheduled repaving of the ETH Extension in Year 5. Assuming this repaving would impact approximately 5% of the road, as per the discussion with the NRA, the resulting risk is quantified at $0.1m (in NPV using a 3.5% discount rate).

As for the ETH Expansion, the sum of risks above is $0.5m, of which $0.1m is allocated to DRCL and $0.5m to the NRA.

In total, the NRA Agreement represents $3.4m of risks assumed by DRCL which are a benefit for CIG and $0.6m of risks assumed by the NRA which are a cost for CIG.

6.2. Qualitative assessment of non-quantifiable risks

PwC believes the NRA Agreement contains a number of ambiguous or insufficiently defined clauses. The NRA Agreement could also have an unintended impact on other aspects of the Cayman Islands economy. Implementation of the NRA Agreement also presents some challenges to CIG which could have financial and/or reputational impacts. These issues and their related risks are discussed below. Because of their nature, it is not possible to quantify these risks, albeit this does not diminish their potential importance over the medium- and long-term.

6.2.1. Type and location of DRCL development

Except for the SMB Hotel, the NRA Agreement does not oblige DRCL to undertake any specific type of development. Although the DRCL Development Plan does foresee a number of new hotels, actual development will depend on market conditions and DRCL's commercial priorities. As a result of the limited specificity in the original version of the NRA Agreement, there were no restrictions which could prevent the following alternative outcomes from occurring:

- DRCL concentrates its development work for the next few years on office and commercial space at Camana Bay and applies the entire $24m Abatements to such development, which arguably would have been viable even without the $24m Abatements; or
- Other than the SMB Hotel, DRCL uses all of the land parcels adjacent to WBR for condominiums instead of hotels.

Either of these outcomes would result in significantly lower economic benefits than those estimated from the hotel/tourism focused projects included in the DRCL Development Plan. Economic benefits to the Cayman Islands could therefore be significantly below those calculated in Section 5 of this report.

However, it is noted that, under the Second Amendment of the NRA Agreement, the incentives schedule includes new parameters for eligibility of development in lands adjacent to the West Bay Road Legal Closure for incentives; specifically, such development will only be eligible for stamp duty, development fees and import duty waivers where it is:

> *"predominantly hotel/tourist resort-oriented, along with ancillary projects such as condominiums, associated real estate and other amenities."*

Given Camana Bay's substantial existing leased commercial property portfolio and the displacement effects on commercial property elsewhere in Grand Cayman, tax incentives on the associated leases are not required. Accordingly, following the Third Amendment, Camana Bay leases will no longer be eligible for relief under the $53m Abatements.

Accordingly, while these changes impose no additional restriction on land use and cannot ensure all incentives will be used to encourage incremental activity, the tax waivers are now better designed to encourage optimal use, from CIG's perspective.

6.2.2. Timing of the DRCL developments

The NRA Agreement only obliges DRCL to start work on the SMB Hotel within 12 months of the date of the Agreement and to continue work until the SMB Hotel is reopened. DRCL has no other obligations to carry out other tourism, real estate or commercial developments within a certain timeframe.

The most important concessions to DRCL have no time limit (the WBR closure cannot be reversed, the $53m Abatements are available until entirely used and effectively increase in value at the equivalent of the annual

10% discount rate) while others are available for a very long period (the Hotel Tax Rebate can be applied to hotel development over the next 30 years). DRCL is therefore able to delay any of the discretionary developments outlined in the DRCL Development plan (aside from the SMB Hotel) until the optimum economic conditions are prevailing, or indeed chose not to undertake them at all. It is therefore possible that the full economic benefits expected by CIG will not occur as quickly as anticipated.

6.2.3. Cost to CIG of the Hotel Tax Rebate

The Hotel Tax Rebate is applicable to "all hotels developed, redeveloped, renovated or refurbished by DRCL or Affiliate for a period of 10 years after each hotel is opened, reopened or renovations or refurbishments are completed"[51]. The hotel tax 10 year rebate applies to any hotel developed or redeveloped/refurbished within a thirty year period, thus creating a potential forty year period from signing of the agreement during which rebates may be earned. The Third Amendment of the NRA Agreement provides further detail on the application of the refurbishment/ renovation definition, namely:

- A qualifying refurbishment shall comprise at least $50,000 per room, based on total rooms in the respective hotel or expenditure of at least 15% of fair market value, based on an independent valuation;
- Refurbishment expenditure can be incurred over a maximum of 24, absent Force Majeure; and
- In the event a hotel receives the initial Hotel Tax Rebate period on construction, it shall be eligible for no further rebates.

The NRA Agreement does not include a definition of "fair market value" nor was CIG able to provide PwC with its own definition. DRCL has advised[52] however, that in its view fair market value would exclude the cost of land.

The Second and Third Amendments have addressed a number of uncertainties and risks associated with the Hotel Tax Rebate arrangements. However, because of the uncertainty concerning under what conditions, and to what hotels, the Hotel Tax Rebate will be applied, it is not possible to determine whether CIG will receive VfM for this concession to DRCL. PwC also understands that CIG has never provided a similar hotel tax rebate to other hotels, so no comparison is possible. Although CIG has in the past negotiated other incentives with hotel developers on a case by case basis, there is clearly a risk that the Hotel Tax Rebate could set a new precedent in the Cayman Islands, which would weaken CIG's negotiating position with alternative potential hotel investors. PwC also notes that, in light of the newly proposed increase in Hotel Tax rates across the board, the Hotel Tax Rebate is now more valuable to DRCL than was the case during the original NRA Agreement negotiation.

6.2.4. Lack of definition of minimum threshold of Caymanian input, including labour

The economic benefits of the NRA Agreement depend, in part, on the use by DRCL of local material and labour during both construction and operation of the road infrastructure and commercial developments. This is particularly true of the employment of Caymanians at the DRCL hotels, the most labour intensive element of the plan. The DRCL Development Plan assumes that circa 64% of employees will be Caymanians, which is significantly higher than at comparable hotels. However, while the Third Amendment includes provisions designed to encourage Caymanian participation, the NRA Agreement does not establish a minimum threshold for local employment or content. As a result, it is difficult to forecast the economic benefits of the NRA Agreement resulting from the employment of Caymanians with any certainty.

[51] NRA Agreement, page 16 of 16 of the appendices
[52] DRCL response to VfM Information Request, received 31 August 2012 and PwC meeting with DRCL on 10 September 2012

6.2.5. Monitoring and maintenance of complex civil structures on the ETH

As noted in Section 6.1.1, DRCL plans to include an overpass structure as part of the ETH Extension. Following the handover at ETH completion, the NRA will be responsible for future maintenance and monitoring of these structures. An estimate of the likely cost of ongoing maintenance has been included in Section 4.2.4 of this report.

However, given that there are no existing structures with this level of complexity in the Cayman Islands, the NRA notes that its expertise in this field is limited. Accordingly, it may be necessary to commission periodic inspections using external expertise and this represents a non-quantified risk for CIG.

6.2.6. Wider impact on tourism and construction

DRCL will benefit from significant advantages as a result of the NRA Agreement, in particular the $53m Abatements and the Hotel Tax Rebate. It is difficult to foresee the impact that these DRCL advantages will have on competing hotel properties. It is possible that the competitive advantage could result in greater than expected displacement from existing hotels. This could have two possible consequences for CIG:

- Lower employment at existing hotels should they reduce operations or close following completion from new DRCL hotels; and
- Lower CIG revenue should occupancy at existing hotels (which pay the full hotel tax) be substituted by occupancy at DRCL hotels (which only pay 50% of the hotel tax because of the Hotel Tax Rebate).

Similarly, the $53m Abatements provide DRCL with construction cost advantages, reduced stamp duty for Caymanians in residential homes adjacent to Camana Bay and (with the exception of Camana Bay) lower lease costs. In combination, there is a risk that these competitive advantages could result in displacement from existing residential property developers and commercial property lessors. However, it is noted that in practice the key source of competitive advantage in both commercial and residential property is location.

6.2.7. Control over import duties and other abatements

Import duty waivers provided under the NRA Agreement can be claimed not only by DRCL but also by any of its affiliates or subcontractors. PwC understands that CIG's control over import duty abatements is based predominantly on the good faith of the declaration made by claimants and periodic spot checks. Given the unprecedented size and scope of the proposed development and associated waivers, there is therefore a risk that import duty abatements are inappropriately claimed by non-qualifying parties and/or for non-qualifying development.

The $53m Abatements cover stamp duty, development fees and import duty. These different fees and duties are collected by different CIG departments and agencies. PwC understands that these departments do not share a common database. It is therefore very important for CIG to put in place a mechanism to ensure that claims made under the $24m Abatements do not surpass the limit set out in the NRA Agreement. This is particularly true given the need to address the added complexity of the unused portion of the $24m Abatements effectively growing at 10% p.a. in nominal terms.

6.2.8. Airport capacity

According to the discussions with the Department of Tourism, developing Grand Cayman's tourism product beyond current demand would require infrastructure investments, in particular an increase in the capacity of the Owen Roberts International Airport. If DRCL proceeds with the entire DRCL Development Plan, it will build five additional hotels during the next ten years, adding approximately 53% to the current hotel offering. The tourism volume needed to take up this supply could require significant airport investment by CIG. PwC understands that the Cayman Islands Airport Authority is conducting an appraisal of alternative financing and

delivery methods for airport redevelopment required for, inter alia, the Shetty Hospital agreement. However, the cost of such an investment or its sources of funding have not been included by PwC in its analysis.

6.2.9. Procurement-related risks

In normal circumstances, whereby road infrastructure is carried out by the NRA, all of the NRA's road construction costs, and sub-contracted works, over a de minimis limit, would be subject to the detailed oversight of CIG's Central Tenders Committee ("CTC"). Within the CIG, CTC's role is an essential mechanism to ensure public funds are properly and transparently spent. By transferring the responsibility for the Road Infrastructure construction to DRCL, CIG is effectively putting the Road Infrastructure expenditure outside the scope of CTC's, and therefore the public's, review. It should be noted that this approach is standard practice for PPP arrangements internationally, in which Governments contract for the delivery of an 'outcome' and the means of delivery is essentially left to the private contractor. However, given CIG's close cooperation with DRCL under the FCIA, there is inherent reputational risk for CIG should DRCL's procurement process fail to meet usual CIG standards around potential or perceived conflicts of interest.

6.2.10. NRA Agreement break fees and damages

In case of termination of the NRA Agreement by the CIG as a result of DRCL default, DRCL must reimburse any value uplift received as a result of CIG actions pursuant to the NRA Agreement. In case of a liquidation of DRCL, CIG may not be able to recoup the value uplift, albeit if the properties are acquired and developed by other parties, the economic benefits would still accrue. It is also unclear how the various rebates may be transferred to other entities either in the case of the sale of DRCL or liquidation for the benefit of creditors, and what are the CIG's rights to secure reimbursement of amounts due in accordance with the NRA Agreement.

6.2.11. Pedestrian and bicycle path

The Second Amendment includes a commitment for DRCL to *"provide pedestrian and bicycle paths for use by the public in perpetuity on the Public Beach Lands and through [those] parts of its land West of the ETH."*

The proposed route of these pathways is set out in an appendix of the Second Amendment, for illustrative purposes. However, this commitment stops short of any registration of new public rights of way on DRCL land and the actual pedestrian and bicycle path routes remain subject to variation. DRCL requires the right to alter the pedestrian and bicycle path's route since its layout for development of hotels and other facilities is not finalized and may not be finalized for a number of years.

The Third Amendment includes further provisions to ensure that the stretch of bicycle and pedestrian path from the Public Beach Park to Raleigh Quay will remain West of all major structures and within 200 feet of the high water mark.

DRCL has advised that the pedestrian and bicycle path routes are fully in-keeping with its overall tourism development plans. However, taken in the context of the Second Amendment's waiving of existing and future prescribed rights of way over DRCL lands in the relevant area, as well as the prohibition on CIG seeking to reinstate any portion of the West Bay Road (refer c.27.7 NRA Agreement), it would appear that the route and extent of an important public amenity will remain at the discretion of a private sector entity. As set out in Section 9, CIG could seek to enhance its control over this public amenity, without encroaching unduly on DRCL's need for commercial flexibility.

6.2.12. Delivery of Government programmes

The Second Amendment of the NRA Agreement provides for DRCL to transfer land to support future CIG initiatives; namely, the Sunrise Adult Training Centre and lands within DRCL's West Bay properties for 'Educational and Community Purposes'.

In light of the current fiscal constraints on the CIG, outlined further in Section 7, there is a risk that public funding for these programmes may not be available in the short to medium term. As such, the lands transferred by DRCL may not actually provide additional public amenity for some time.

Further, with respect to the Sunrise Adult Training Centre, it is noted that, given the likely location of the lands to be transferred, a new access route will be required to the nearest public highway. DRCL has advised that it would intend to provide such access without charge, albeit the terms of the Second Amendment itself are not clear regarding whether DRCL has a strict obligation in this regard.

6.2.13. DRCL financial capacity

No assessment of DRCL's financial capacity was conducted during the preparation of this report. A significant portion of the NRA Agreement is predicated on DRCL's capacity to fund substantial investment to complete both its direct contractual obligations (such as the ETH Extension and SMB Hotel) and its non-binding development plan.

6.2.14. Pedestrian Crossing at Camana Bay

The NRA Agreement allows DRCL, at its expense, to build an "in-road warning-light pedestrian crossing, demarcated with alternate road surfacing at ETH and Camana Way". The NRA has expressed a concern about the safety of such a crossing for pedestrians and motorists given the traffic volume and speeds on the ETH.

6.2.15. Coastal Works / Compensatory Mitigation

The Third Amendment includes provisions for when DRCL is assessed compensatory mitigation for sensitive habitat loss under a Coastal Works Licence or Coastal Works Permit.

The impact of these provisions and the extent to which they modify CIG's standard approach in similar situations is not clear for PwC. We do note however that:

- These provisions require DRCL's agreement, which may limit CIG's ability to act; and
- There is no limit on these provisions, either in time, their location or the type of project they are applicable to.

7. CIG alternatives to the NRA Agreement

7.1. Introduction

The Terms of Reference require PwC to consider the alternative options for delivery of road infrastructure, in the absence of the NRA Agreement. Specifically, CIG requires PwC to:

> *"Identify the realistic alternatives available to the CIG to finance the construction of the road infrastructure defined in Schedule 1 by December 2013. Realistic alternatives must be in compliance with the FFR, the CIG's Fiscal Strategy, and the Public Management and Finance Law."*

Schedule 1 of the Terms of Reference defines the road infrastructure ("Road Infrastructure") as follows:

> *"a. The extension of the Esterley Tibbetts Highway to Batabano Road;*
> *b. The construction of Reverend Blackman Road west of the Esterley Tibbetts Highway to Willie Farrington Drive; and*
> *c. Construction of the Barkers Road."*

As such, the analysis below considers options for delivery of the Road Infrastructure in its proposed form. The Third Amendment also includes provision for the ETH Expansion which, while not included in the Terms of Reference definition of the Road Infrastructure, comprises an additional public infrastructure enhancement. In setting out these options it should be highlighted that these alternatives may, and in most cases probably will, offer reduced beneficial economic impacts relative to the full NRA Agreement, which incorporates the SMB Hotel construction and incentivizes further additional development.

Aside from tolling, this analysis does not consider potential new revenue raising measures available to CIG, such as property taxes, on the basis that taxation policy is outside the scope of the Terms of Reference.

7.2. Traditional delivery method and CIG's fiscal constraints

7.2.1. Traditional delivery method

The NRA acts both as the primary road constructor and maintainer in Grand Cayman, but where necessary will outsource both road construction and maintenance projects to the private sector on a competitive tender basis. As such, road construction by the NRA represents the 'Traditional Delivery' method for roads in the Cayman Islands.

The NRA was created on 1 July 2004 with the broad remit to administer, manage, control, develop and maintain the Islands' public roads and related facilities, such as signals, storm water facilities, roadway lighting and roadway directional signage.

The NRA's constitution, funding and authority is principally governed by the NRA Law 2004 and its other activities are largely governed by the Roads Law 2005 Revision and the Traffic Law 2003.

A board of directors, appointed by the Governor in Cabinet, governs the NRA. The Minister responsible for the authority may also give general policy directions to the board. The board is then responsible for enacting NRA policy and the general affairs and business of the authority.

The 2004 NRA Law included provision for a Road Fund, which allocates a proportion of four categories of Government revenue income to fund the NRA, specifically:

- 20% of the duty collected on motor gasoline imported into the Islands
- 16 2/3 % of the duty collected upon diesel oil imported into the Islands, (excluding diesel used by Caribbean Utilities Co. ltd.)
- 100% of the fees paid to the infrastructure fund, as outlined in the Development and Planning Law (2003 Revision).
- 80% of the fees paid in respect of the registration of motor vehicles under Part II of the Traffic Law (2003 Revision).

In practice however, even in the absence of major road building programs the NRA also requires substantial further funding from core government in addition to the revenue stream allocations above, in order to meet annual operating and investment budgets.

Consequently, the NRA is not in a position to fund the construction of the proposed Roads Infrastructure without the appropriation of substantially all of the associated financing from core government.

7.2.2. CIG's fiscal constraints

Since the onset of the global financial crisis, the public finances of the Cayman Islands have been severely adversely impacted by erosion of core CIG revenue streams from the financial, real estate and tourism sectors. In addition, ongoing capital projects and the size of the public sector cost base have placed further pressure on public finances.

Core CIG revenues only marginally exceeded expenses in 2011/2012, following a number of years of deficits. While PwC understands that a small surplus is expected for 2012/13, total public sector debt is still expected to rise to in excess of CI$700m at the end of fiscal year 2012/2013.

While ratings agencies have recently confirmed the Cayman Islands' rating at Aa3, indicating that CIG retains some borrowing capacity, this rating is predicated on prudent fiscal management. In particular, CIG's fiscal management is strictly governed by the provisions of the Public Management and Finance Law (Revised) ("PMFL") and the guidance and principles set out in the CIG's Framework for Fiscal Responsibility ("FFR").

The PMFL sets out, at s.14(3), six principles of responsible financial management, namely:

> *"(a) total core government revenue less total core government expenses (measured using generally accepted accounting practice) should be positive;*
>
> *(b) total core government assets less total core government liabilities (measured using generally accepted accounting practice) should be positive;*
>
> *(c) borrowing should not exceed an amount for which the sum of interest, other debt servicing expenses and principal repayments for a financial year are more than ten per cent of core government revenue (calculated using generally accepted accounting practice) for that financial year, where, for the purposes of this principle, borrowing is defined as all borrowing that is in the name of the Government regardless of whether it is serviced directly by the core government, a statutory authority or government company;*
>
> *(d) net debt should be no more than eighty per cent of core government revenue, where, for the purposes of this principle, net debt is defined as -*
> *(i) core government borrowing less core government liquid assets;*
> *(ii) borrowing that is serviced directly by a statutory authority or government company but is in the name of the Government; and*
> *(iii) the percentage of statutory authority and government company debt guaranteed by the Government that regulations made under this Law specify is to be included in the net debt calculation;*
>
> *(e) cash reserves should be maintained at a level no less than the estimated executive expenses (measured using generally accepted accounting practice) for the following ninety days, where, for the purposes of this principle, cash reserves are defined as core government cash and cash*

equivalents, marketable securities and deposits, and other liquid assets, including any amounts held for restricted funds and reserves purposes; and

(f) the financial risks, including contingent liabilities, facing the core government should be managed prudently so as to minimise the likelihood of any such risk resulting in an expense or liability."

Of these six principles, PwC understands that three are currently in breach, specifically:

- S.14(3) c: Total Debt service costs currently exceed 10% of core government revenues;
- S.14(3) d: Net debt as defined above currently exceeds 80% of core government revenues; and
- S.14(3) e: Current cash reserves are insufficient to meet the following ninety days of estimated executive expenses.

One result of these breaches of financial management principles, which have been ongoing for a number of years, is a limitation on the permissible quantum of CIG borrowings ("the Borrowing Limit"). This limitation was proposed by the UK's Foreign and Commonwealth Office ("FCO") and accepted by the CIG. At present, the CIG has exhausted the permissible borrowings under the existing Borrowing Limit.

The FFR, which was agreed in November 2011, was developed in part in order to provide a framework for addressing the recovery of the Cayman Islands public finances over the medium term, and its provisions were reflected in an amendment to the PMFL.

The FFR recognizes that the ongoing impact of the global financial crisis and resulting recession will effectively prevent adherence to the PMFL's financial management principles for some time. Accordingly, transitional provisions are set out in the FFR's Annex D, which require compliance with Debt Service, Net Debt and Liquid Asset tests (S.14(3) c, d, and e respectively) by 2015/2016. PwC understands that during this period, CIG will also need to establish a sinking fund to provide for amortizations of any interest-only CIG debt. Following the FCO's role in recent revisions to CIG's 2012/13 budget, in future it is widely reported that the FCO's role in monitoring of CIG budgets and public spending will be increased.

In summary, CIG is required to carry out a significant fiscal retrenchment over the next three financial years.

Given that there are a number of existing capital commitments on the Cayman Islands public purse, most notably the John Gray and Clifton Hunter High Schools, it is likely that any additional borrowing sanctioned by CIG and the FCO, would need to address these priorities.

As such, in the circumstances, general prudent fiscal management as well as the provisions of the PMFL and the FFR would likely preclude raising new debt finance for Traditional Delivery of the road infrastructure by December 2013.

7.3. Options

In considering the realistic alternatives for delivery of the Roads Infrastructure by 31 December 2013, the fiscal constraints noted above must be borne in mind; that is, financing for the Roads Infrastructure would need to be funded by a third party, with no resultant additional debt obligations on CIG, as defined by the PMFL and FFR.

7.3.1. CIG building the Roads Infrastructure itself and selling West Bay Road closure to DRCL

The NRA Agreement is essentially a barter arrangement, whereby CIG swaps a strip of WBR land, plus a series of incentives, for construction of the Roads Infrastructure, a cash payment, transfer of DRCL land to CIG, and the future economic benefits and job creation from improved tourism capacity, and product, in the Cayman Islands.

An alternative approach would be to separate the core elements of the NRA Agreement. Under this approach, the WBR land would be sold to DRCL in an arms' length transaction for cash consideration. In negotiating a

price for this land, CIG would no doubt be mindful of the value uplift and the precedents for recovering an element of this value uplift for the public (as discussed in Section 4). Further, under this approach CIG may also choose to offer taxation incentives specific to the SMB Hotel and adjacent WBR land parcels, both in order to incentivize development and to maximize the price offered for the land by DRCL.

CIG should then be in a position to use the proceeds from the land sale to fund its own construction of the Roads Infrastructure, using the NRA under the Traditional Delivery method.

Potential advantages of this approach would include CIG and NRA retaining greater control over the Roads Infrastructure procurement and delivery, improved transparency over the actual price being paid for the strip of WBR land and also the separation of wider taxation incentives from the specific elements related to WBR closure and the Roads Infrastructure.

However, there are potential disadvantages to this approach, including:

- It remains uncertain whether DRCL would be willing to offer a cash price acceptable to CIG for the West Bay Road land. In the current economic climate, and in light of the intensely competitive regional market for tourism, CIG would be negotiating from a position of relative weakness; and
- Under this approach, the NRA, rather than DRCL, would bear the full construction risk of the Roads Infrastructure. This risk could be exacerbated by the need to ensure the ETH Extension in particular allows proper access and flexibility for future tourism development, which is identified within the Terms of Reference as a key infrastructure need. Under the NRA Agreement, DRCL is responsible for the cost and risk associated with ensuring proper access for future tourism development in the land holdings adjacent to the ETH Extension. Given that DRCL owns these land parcels, this approach would seem logical.

In summary, while greater transparency and control would be desirable, particularly in terms of taxation incentives, it is not necessary to fully separate the elements of the NRA Agreement to achieve this. This issue is discussed in further detail in Section 9.

7.3.2. CIG entering into a property sale or development agreement with an alternative counterparty

DRCL's land holdings along the relevant sections of WBR result in DRCL being the sole potential counter-party for a transaction involving the closure of that portion of WBR.

Similarly, DRCL's land holdings adjacent to the proposed Road Infrastructure effectively mean that no other third party holds sufficient commercial interest in the Road Infrastructure to offer CIG incentives to construct. Indeed, given that the ETH Extension has long been part of CIG's infrastructure plans it would be highly unusual for a private third party to fund construction of a major planned public highway.

CIG does have the option of reviewing its other land holdings in the Cayman Islands to consider whether sales of alternative land parcels to third parties could raise sufficient proceeds to fund the Road Infrastructure.

However, it should be noted that the closure of the relevant portion of WBR delivers a unique synergy value to the counter-party, through the provision of beach access to the inland DRCL land holdings. This synergy value is shared by CIG under the NRA Agreement. The West Bay Road corridor represents the core high value tourism real estate in the Cayman Islands and, aside from the land parcels considered in the NRA Agreement, this corridor is now largely developed. Therefore, it is likely that this unique synergy value would not be available elsewhere in the Cayman Islands nor to any counterparty other than DRCL.

As such, in order to generate the funds required for the Road Infrastructure, CIG would likely have to sell significant tracts of public land elsewhere. Indeed, it is uncertain whether there would be sufficient market for such land holdings outside of the WBR corridor, particularly in the absence of the type of development incentives offered by the Cayman Islands' competitor jurisdictions in the Caribbean region, such as casino licenses.

Furthermore, it should be noted that a land transaction with an alternative counterparty may not offer the economic benefits and enhancement of tourism product identified under the NRA Agreement.

7.3.3. ETH Extension as a Public-Private Partnership

Public-Private Partnership ("PPP") is a generic term which covers a wide range of procurement models for infrastructure projects such as hospitals, public amenities, transport infrastructure and educational facilities.

The basic tenet of PPP is that, through an optimal allocation of risks and responsibilities related to infrastructure and service delivery between private and public sector participants, governments are able to reduce the 'whole-life' cost of providing the services and/or improving the quality of service provision.

PPP contracting has evolved since its inception in the UK two decades ago, and it is now widely recognised that the principal driver for a successful PPP transaction must be its inherent value-for-money in terms of risk transfer and potential for 'whole-life' savings, rather than accounting treatment.

7.3.3.1. Accounting Treatment

It should be highlighted that CIG's PPP options for delivery of the Road Infrastructure are limited by their potential impact on the Borrowing Limit, discussed at 7.2.2 above.

In particular, where a proposed PPP model requires recognition of the associated public sector obligations as debt, this will effectively prevent CIG from adopting this PPP model, for much the same reasons CIG is unable to raise additional debt funding for Traditional Delivery of the Roads Infrastructure.

Under the PMFL's Financial Regulations (2004), CIG's public sector accounts are reported under International Public Sector Accounting Standards ("IPSAS"). Where IPSAS is silent, International Financial Reporting Standards ("IFRS") are used and UK Generally Accepted Accounting Principles ("UK GAAP") represent the final source of guidance, if IPSAS and IFRS do not provide guidance.

IFRIC 12 ("International Financial Reporting Interpretations Committee, Interpretation 12") is the IFRS accounting guidance which specifically deals with Service Concessions and is therefore most relevant to PPP accounting models. This guidance determines how a private sector PPP contractor should account for its borrowings and construction assets and, in contrast to prior standards, is based on an assessment of control, rather than risk transfer.

For resource accounting purposes only, UK government departments use a 'mirror-image' of the IFRIC 12 guidance to private contractors to determine the corresponding public sector accounting treatment for Service Concessions.

In determining which party has effective control over an infrastructure asset, IFRIC 12 considers factors such as:

1. The source of revenues to the PPP contractor; that is, is the contractor dependant on the public sector for payments under the arrangement?
2. If any revenues are sourced from elsewhere, to what extent is the government able to regulate and control pricing charged to users? and
3. Who has control over the residual interest in the asset at the end of the concession period?

Where government provides revenues or fully controls them through regulation, and where government controls the residual interest in the asset, it is determined to have retained the overall control of the asset by determining how it is used for its entire useful economic life, and, as such, the borrowing remains 'Off Balance-Sheet' for the contractor under IFRIC 12, and therefore 'On Balance-Sheet' for government under the 'mirror-image' used by the UK Government

These accounting criteria present a relatively high commercial hurdle to overcome in order to achieve 'Off Balance-Sheet' treatment for government.

Essentially, under IFRIC 12, the only Service Concessions eligible for 'Off Balance-Sheet' treatment are those that can operate as a stand-alone commercial venture, with the need for only limited government regulation to avoid monopolistic pricing.

This position is reinforced by the definition of *'Public Borrowings'* included in Annex A of the FFR, which states that 100% of debt will be recognized for:

> *"Outstanding contractual commitments to PFI [Private Finance Initiatives] or PPP arrangements of any form…"*

The practical implication of this accounting treatment is that commonly used road PPP models such as the 'Availability Model' (in which Government makes periodic payments to the contractor linked to road availability criteria) and the 'Shadow Tolling Model' (in which Government's periodic payments are linked to assessed road usage volumes) would be deemed to leave ultimate control of the asset with CIG and would therefore result in recognition of future PPP obligations as debt for CIG.

As such, these PPP models for roads would not be available to CIG in light of the existing fiscal constraints.

Remaining alternative models would include the 'Real Tolling / User Pays' model (in which actual tolls are levied on road users), and the 'Tied-in Concession' model (in which Government grants a PPP contractor a concession to construct and operate a revenue generating asset, in conjunction with the roads concession). Each of these models can, in the right commercial circumstances, operate as viable stand-alone enterprises, and enable transfer of both risk and control to the private sector contractor.

7.3.3.2. Commercial Viability

In considering commercial viability of the Real Tolling or Tied-in Concession models for the Road Infrastructure, it is important to note that the size of the project, at c $37m, is relatively small in the context of PPP projects. Adding the ETH Expansion costs of $10m does increase the potential size of the PPP but it would continue to be considered small.

PwC has previously conducted market sounding processes to gauge appetite for PPP in the Cayman Islands and these results indicate that, while there is appetite to finance and deliver infrastructure PPP in the Cayman Islands, a project of this size would likely be too small to attract credible and experienced international PPP contractors.

Clearly, there are Cayman Islands based contractors with the technical and engineering capacity to deliver the Roads Infrastructure. However, delivery of complex PPP arrangements, particularly those involving transfer of control and volume / demand risk, requires contractors with a depth of experience in such projects, as well as access to the requisite long term funding. The previous discussions with local providers indicate that this level of experience and appetite to wholly fund long term PPP projects is limited on-island, and in fact the preferred approach would be partnership with international PPP contractors.

As a result, it is questionable whether there would be a market appetite among contractors or financers to deliver a PPP in the Cayman Islands for the Roads Infrastructure alone.

With respect to the Real Tolling model, the commercial viability of any tolling arrangement is a function of the costs of construction, operation and maintenance, versus the level of revenues that can be generated from the associated traffic. Accordingly, factors impacting commercial viability will include:

1. Projected traffic volumes;
2. Potential 'leakage' of traffic through alternative routes'
3. Cost of revenue collection; and
4. Costs of construction and ongoing maintenance.

PwC has examined NRA road user volume data and draws a high level conclusion that, even before accounting for the costs of ongoing road maintenance and the considerable cost of revenue collection (including uncollectables), traffic estimates and potential associated revenues appear insufficient to fund a Real Tolling PPP solution for the Road Infrastructure.

Experience elsewhere indicates that, given the substantial cost of implementing tolling, substantial sustained traffic volumes are required in order to make tolling arrangements practically and commercially viable. As such, it appears that real tolling may not be a viable option for delivery of the Roads Infrastructure. This is further exacerbated by the current market view of tolling risk as a result of the global recession.

With respect to the Tied-in Concession delivery model, commercial viability will largely depend on the ability of the combined concessions to be independently financially sustainable on a stand-alone basis, with no contribution from Government.

As such, given the cost of the proposed PPP projects, it is likely that any associated revenue generating concession would need to be a substantial venture. Accordingly, fuelling / service stations would not be sufficient on their own.

In effect, the NRA Agreement is itself a form of Tied-in Concession arrangement, albeit rather than providing a concession CIG has instead agreed to the closure of a portion of WBR in order to enable the reopening of the SMB Hotel and potential further development.

Tied-in Concessions would ordinarily comprise substantial transport infrastructure, such as airports and ports, or possibly sports stadia or casino concessions. Accordingly, there does not appear to be a realistic alternative option for a substantial Tied-in Concession along the route of the Road Infrastructure, particularly in light of DRCL's extensive adjacent land holdings.

In conclusion, as a result of both fiscal constraints and commercial viability issues, delivery of the Road Infrastructure outlined in Schedule 1 of the Terms of Reference through a PPP arrangement by 31 December 2013 does not appear to be a realistic option.

8. Compliance with the FFR

8.1. Introduction

The Terms of Reference require an assessment of the NRA Agreement's compliance with the FFR. Specifically, CIG requires:

> *"An assessment of the Agreement's compliance with the FFR. Compliance with the Government's FFR shall be assessed by the Independent Reviewer in terms of the Government's Fiscal Strategy consisting of the following five components:*
> - *Controlling Government Expenditure;*
> - *Management of Public Debt;*
> - *Revenue Enhancement;*
> - *Financial Improvement of Statutory Authorities and Government Companies; and*
> - *Public Private Partnerships."*

As noted in Section 7, the FFR was agreed between CIG and the FCO in November 2011 and provides a set of guiding principles for the restoration of prudent fiscal management in the Cayman Islands. The FFR provides guidelines, whereas the PMFL provides detailed financial management requirements.

With respect to capital projects, such as the NRA Agreement, the FFR provides guidelines for both the appraisal and procurement process undertaken to execute the project, as well as the fundamental commercial terms and associated risks of the proposed project. The core policy principles outlined in the FFR comprise:

1. Effective **medium-term planning**, to ensure that the full impact of fiscal decisions is understood;
2. Putting **value for money** considerations at the heart of the decision making process;
3. Effective **management of risk;** and
4. Delivering improved **accountability** in all public sector operations.

Accordingly, in an assessment of compliance with the FFR, one must have regard to the core policy principles and the appraisal and procurement process undertaken by CIG, as well as the actual terms of the NRA Agreement.

8.2. Controlling Government expenditure

In simplistic terms, the NRA Agreement generates minimal public sector expenditure obligations, other than the initial NRA costs of overseeing road construction and their ongoing costs in maintenance of the new Road Infrastructure.

However, as highlighted earlier in this report, the NRA Agreement is effectively a barter transaction, or arguably a joint venture, in which CIG is exchanging valuable land synergies and taxation incentives for the roads infrastructure and future economic benefits.

As such, CIG is paying for the ETH Extension, albeit with non-cash consideration. The principle purpose of this review is to assess the VfM aspects of this transaction. In non-standard transactions such as the NRA Agreement, where there is only one possible counterparty, the VfM review is a critical tool for protecting CIG's interests and is in fact mandated by the FFR. The FFR's project appraisal requirements under PPP / alternative finance transactions are discussed further in Section 8.6 below.

In normal circumstances, under the Traditional Delivery method, all of the NRA's road construction costs, and sub-contracted works, over a de minimis limit, would be subject to the detailed oversight of CIG's CTC. Within

the CIG, CTC's role is an essential mechanism to ensure public funds are properly and transparently spent. By transferring the responsibility for the Road Infrastructure construction to DRCL, CIG is effectively putting the Road Infrastructure expenditure outside the scope of CTC's, and therefore the public's, review. However, it should be noted that this approach is standard practice for PPP arrangements internationally, in which Governments contract for the delivery of an 'outcome' and the means of delivery is essentially left to the private contractor, subject to proper disclosure of any potential or perceived conflicts of interest by all parties.

8.3. Management of public debt

Section 7.2.2 above provides a detailed background on the fiscal constraints faced by the CIG. In summary, it has been widely reported that, principally as a result of revenue erosion following the global financial crisis, as well as major recent and ongoing capital projects and the size of the public sector cost base, the public finances of the Cayman Islands are severely constrained. General prudent fiscal management as well as the specific provisions of the PMFL and FFR would preclude CIG taking on new borrowings to fund the Roads Infrastructure, in the near to medium term.

The NRA Agreement, by allowing CIG to capture a portion of the value uplift from the WBR closure, enables the financing of the Roads Infrastructure without any additional public debt. Accordingly, under both IPSAS and IFRS the terms of the NRA Agreement would not create any additional public debt burden. The closure and divestment of a section of WBR would be treated as an asset disposal. However, in light of the related acquisition of the new Road Infrastructure, the overall impact on CIG's net asset position under PMFL s.14(3) b is likely to be positive, albeit this is dependent on the valuation policies CIG adopt with respect to these exchanged road assets.

8.4. Revenue enhancement

As outlined in Section 5 above, the anticipated economic impact of the NRA Agreement is expected to be substantial. The FFR identifies re-alignment of CIG's revenue base as one of the five components of fiscal strategy. In this respect, the impact of the NRA Agreement can be viewed as likely to bolster and diversify the Cayman Islands' tourism product and in doing so support overall GDP growth and reduce reliance on financial services in CIG's revenue base.

PwC's interviews with the Department of Tourism confirm the need for increased hotel room capacity in the Cayman Islands and, in particular, the significant benefit of attracting a major tourism brand, with all the associated marketing profile. The view that there is an unfilled niche in the tourism market is also corroborated by the REVPAR Report commissioned by DRCL.

Clearly, the anticipated benefits to the Cayman Islands economy must be tempered by the taxation incentives included in the NRA Agreement. The impact of these incentives is discussed in further detail in Section 9.

8.5. Financial improvement of statutory authorities and Government companies

This element of CIG fiscal strategy is principally addressed in the FFR in terms of the robust processes required of Government bodies to measure performance, allocate budgets, determine revenue targets, assess risks and conduct financial reporting and audits. As such, this area of the FFR's guidelines has limited impact on the terms of the NRA Agreement.

However, it should be noted that the NRA's obligations under the NRA Agreement to oversee construction and maintain the Road Infrastructure following construction, will required appropriate financing from core CIG. Further, the implementation and control over tax incentives included in the NRA Agreement will require robust oversight and cooperation between a number of CIG ministries and statutory authorities.

8.6. Public-Private Partnerships

The NRA Agreement, while not a PPP in the strictest sense, does constitute alternative financing of infrastructure, and as such there are specific provisions within the FFR with respect to the appropriate appraisal process, namely:

> *"PPPs or any other form of alternative financing will only be considered:*
> 1. *where there is a sound appraisal underpinning the proposed project before the financing means has been determined;*
> 2. *where a financial appraisal demonstrates improved value for money against a conventionally financed alternative;*
> 3. *where the long term affordability case has been assessed and agreed by the appropriate technical experts retained by the Cayman Islands Government; and*
> 4. *where an independent opinion has been received from a qualified accountant of good standing on the correct accounting treatment in the Cayman Islands Government's accounts."*

CIG's commissioning of this VfM review, and if appropriate acting on the review's findings, meets a core requirement of the FFR. In non-standard transactions such as the NRA Agreement, where there is only one possible counterparty, the VfM review is a critical tool for protecting CIG's interests. This is particularly the case given that a competitive tender process, and associated price discovery, is not feasible in this scenario.

As set out under the FFR, this VfM review should have been conducted as part of the initial project appraisal at an early stage in the overall process, rather than at this late stage. Further, under the FFR, the CIG's own project appraisal should have been conducted and published for public consultation prior to the procurement stage.

PwC understands that in practice the NRA Agreement evaluation and negotiation was principally carried out by policy makers, as opposed to civil service ministries and departments.

However, it is recognized that the FFR itself was only agreed in November 2011, by which point the NRA Agreement was largely completed, following up to a year of protracted negotiations. The NRA Agreement also includes a provision for the completion of the VfM Review and a process for addressing any associated amendments, which to an extent protected CIG's position.

In addition, while the FFR provides general guidance on approach, it seems that the PMFL's 2004 Regulations do not provide adequate detailed regulations for implementing the FFR's guidance around business appraisal, VfM review and negotiation for non-standard capital transactions with only one potential counterparty. As the NRA Agreement could not feasibly be put out to competitive tender, and is therefore not likely to be subject to CTC review, there does not appear to be a clear route for appraisal and project acceptance within CIG regulations. This is particularly the case given that the Public Sector Investment Committee ("PSIC") envisaged under the PMFL has not been established.

8.7. Conclusion

As discussed in detail at Section 5, the terms of the NRA Agreement are expected to generate substantial positive economic impact for the Cayman Islands, and CIG had the opportunity to secure greater certainty over this benefit by further tailoring the taxation incentives and other terms, as a result of the amendment clauses included in the NRA Agreement.

As such, and based on the likely impacts on public debt and revenues discussed above, the result of the NRA Agreement is expected to be broadly in line with the guidelines under the FFR and CIG's five components of fiscal strategy.

In an assessment of compliance with the FFR, one must have regard to the appraisal and negotiation process undertaken by CIG, as well as the actual terms and expected outcomes of the NRA Agreement.

As set out under the FFR, this VfM review should have been conducted as part of the initial project appraisal at an early stage in the overall process, rather than at this late stage, and the CIG's own project appraisal should have been carried out and published for public consultation prior to the procurement stage.

However, the FFR was only signed in November 2011, toward the end of the NRA Agreement negotiation process. Further, while the FFR provides general guidance on approach, it seems that the PMFL's 2004 Regulations do not provide adequate detailed regulations for implementing the FFR's guidance around business appraisal, VfM review and negotiation for non-standard capital transactions with only one potential counterparty. As the NRA Agreement could not feasibly be put out to competitive tender, and is therefore not likely to be subject to CTC review, there does not appear to be a clear route for appraisal and project acceptance within CIG regulations. This is particularly the case given that the Public Sector Investment Committee envisaged under the PMFL has not been established.

Accordingly, it is recommended that CIG consider amendments to the PMFL and associated Regulations in order to provide for a clear and transparent appraisal and approval process for non-standard transactions, where competitive tender is not feasible. Such amendments should ensure that the process puts responsibility and authority for appraisal and detailed negotiation on the civil service, drawing on a cross section of civil service expertise, and thereby enabling policy makers to focus on strategic policy.

It should also be noted that, by transferring the responsibility for the Road Infrastructure construction to DRCL, CIG is effectively putting the Road Infrastructure expenditure outside the scope of CTC's, and therefore the public's, review. This approach is standard practice for PPP arrangements internationally, in which Governments contract for the delivery of an 'outcome' and the means of delivery is essentially left to the private contractor.

However, given CIG's close cooperation with DRCL under the FCIA, there is inherent reputational risk for CIG should DRCL's procurement process fail to meet prescribed CIG standards around potential or perceived conflicts of interest. As such, it is recommended that CIG provide DRCL with guidelines around management and disclosure of any actual or perceived conflicts of interest in their procurement process.

9. Independent Review conclusions and recommendations

9.1. Introduction

This section presents PwC's overall assessment of whether the NRA Agreement provides VfM to the CIG, a summary of the conclusions that can be drawn from this and the other areas of the Independent Review scope, and PwC's key recommendations to the CIG.

The VfM assessment is carried out for each of the three major components of the NRA Agreement as set out in Section 2, namely:

- Infrastructure and SMB Hotel development;
- Stamp duty, development fees and import duty abatements and SMB Hotel Tax Rebate, eligible for the $53m Abatements; and
- Hotel Tax Rebate for other hotels.

9.2. VfM Assessment: Infrastructure and SMB Hotel development

The NRA Agreement provides for significant financial benefits for the CIG in the short term, particularly in the form of road construction to be carried out by DRCL, land to be transferred to CIG by DRCL, improvements to existing and new public beaches and creation of new public pedestrian and bike paths as well as a cash grant which DRCL has already paid to the CIG. The NRA Agreement also allocates risks relating to the construction of the ETH Extension and, partially, the ETH Expansion to DRCL which would traditionally be supported by the NRA. Finally, the NRA Agreement should generate substantial economic benefits for the Cayman Islands from the reopening of the SMB Hotel as well as from the rest of the DRCL Development Plan should it be executed.

In return for these benefits, the NRA Agreement requires the CIG to incur certain costs and divest assets to DRCL. The most important of these is the CIG agreeing to the closure of a portion of the WBR and the vesting of this land to DRCL following the process set out in the Roads Law as well as the extinguishing of DRCL's obligation to provide the public rights of way stipulated under the Cayman Islands Development and Planning Regulations. Ordinarily, where a private developer seeks the closure and vesting of public land to facilitate its development, CIG could require sales proceeds in return, based on a market valuation. Accordingly, the proceeds foregone by CIG in transferring this land represent costs, or forgone assets, for CIG under the NRA Agreement. The NRA will also be required to support monitoring costs relating to the construction of the ETH Extension and New Barkers Road as well as incremental costs and risks relating to the operation of these new roads and of the ETH Expansion.

A summary of these benefits, costs and risks is shown in **Figure 32**.

Figure 32
Summary of the VfM analysis of the infrastructure and SMB Hotel development component of the NRA Agreement ($m)

	Benefits to CIG	CIG Costs / Divestments	20 Year Economic impact, SMB Hotel only	20 Year Economic impact, SMB Hotel and DRCL Development Plan
Financial benefits (ref. Figure 6)	**$78.1**	**$78.2**	**$755**	**$2,447**
Quantified risks transferred to DRCL (ref. Section 6.1.7)	3.4	0.6		
Total	**$81.5**	**$78.8**		

Overall, PwC believes that the infrastructure and SMB Hotel development component of the NRA Agreement provide VfM to the CIG. Not only is the sum of tangible benefits to the CIG (including transferred risks) slightly greater than the sum of CIG costs, divestments and retained risks, the following considerations must also be taken into account:

- The most important contribution by the CIG to the NRA Agreement is the divestment of the closed WBR and Barkers lands, valued at $57.1m representing a share of WBR and Barkers land value uplift for which CIG is foregoing a direct cash compensation. This value uplift, while real, is difficult to estimate and does not constitute an immediate source of cash for DRCL. Further, for DRCL to recoup the value of this uplift requires substantial additional investment in the construction and operation of a major hotel. This represents a relatively high risk venture in the current economic climate. While PwC believes it is appropriate to include this amount among the CIG costs and divestments under the NRA Agreement, it does not require any disbursement of funds by CIG.
- The quantified benefits do not include intangible benefits such as the anticipated improvements to the existing public beach following the closure of the WBR and the creation of the Public Beach Park. However, the quantified costs do not include intangible costs either, such as the potential social impact of reduced beach access to the public along the length of the former West Bay Road.
- Most of the benefits CIG is to receive will materialize in the short term. DRCL has almost completed work on the ETH Extension and has already paid CIG the entire $5m grant.

VfM is also provided to the Cayman Islands from the economic impact and other advantages generated by the NRA Agreement:

- PwC estimates that the net economic impact to the Cayman Islands over the 20 year operational period covered by the economic impact study to be up to approximately $755m if only the SMB Hotel is reopened and up to $2.4bn if the entire DRCL Development Plan is implemented;
- The closure of a portion of the WBR and the construction of the ETH Extension and the ETH Expansion will provide benefits to the Cayman Islands not fully captured in the estimated economic impacts. Most notably, these road projects will be a major step in the NRA's plan to make the WBR better adapted for pedestrians and will help to alleviate congestion. The diversion of traffic from the WBR to the ETH Extension is also expected to contribute to the safety and well-being of Caymanians, albeit concerns have been raised regarding the social impact of potentially reduced beach access to the public;
- The addition of the new hotel brands comprised in the DRCL Development Plan to the Cayman Islands will generate new location specific marketing spend which can be expected to raise the profile of Cayman as a destination and have consequent benefits for the wider Cayman Islands tourism sector.

9.3. VfM Assessment: Stamp duty, development fees and import duty abatements and SMB Hotel Tax Rebate

The $53m Abatements are presented by DRCL as an important component in DRCL's decision to go forward with the DRCL Development Plan. From the perspective of VfM, the rationale for providing these abatements depends largely on the likelihood that they will act as true incentives to spur development and associated positive economic impacts, rather than acting as subsidies for future development that would have been undertaken in any event.

The full scope of investment included in the DRCL Development Plan (excluding the SMB Hotel, which is eligible for separate abatements) totals investment of up to $1.1bn in NPV terms and associated economic impacts of up to $2,447m. In this context the $53m Abatements appear to support VfM. Assuming that DRCL utilizes the $53m Abatements as soon as possible in line with the DRCL Development Plan:

- The DRCL Development Plan, excluding the SMB Hotel, would, if fully implemented, generate on an NPV basis $39m of incremental development fees and duties payable to the CIG after application of the $53m Abatements, which is equal to $162m on a nominal, undiscounted basis;
- To benefit from the full $53m Abatements, DRCL must build the equivalent of the following projects, which represent a total investment of approximately $415m, which are included in years 2012 to 2017 of the DRCL Development Plan:
  - WB Lands Condo 1 (100 units)
  - WB Lands Condos 2 (50 units)
  - WB Hotel 2 (300 rooms)
  - WB Hotel 3 (150 rooms)
  - Eco-Tourism Hotel (100 rooms)
  - Commercial Centre 1 (50,000 square feet)
  - WB Condos 3 (100 units)
  - Commercial Centre 2 (50,000 square feet)
  - Housing development at Crymble Landholdings (partial)
  - Housing development at CIYCAM Lands (partial)

However, except for the SMB Hotel, the NRA Agreement does not oblige DRCL to undertake any specific type of development nor does it establish any guidelines as to the nature, timing or scope of future developments. Although the DRCL Development Plan does foresee a number of new hotels, actual development will depend on market conditions and DRCL's commercial priorities. As a result of the limited specificity in the NRA Agreement, there are no restrictions which could prevent DRCL from concentrating its resources for the next few years on office and commercial space at Camana Bay and applying the entire $53m Abatements to such development, which arguably could have been viable even without the $53m Abatements.

Such an outcome would result in significantly lower economic benefits than those estimated from the hotel/tourism focused projects included in the DRCL Development Plan. Economic benefits to the Cayman Islands could therefore be significantly below those calculated in Section 5 of this report.

PwC believes these shortcomings in the potential application of the $53m Abatement need to be addressed to ensure that the CIG obtains VfM.

9.4. VfM Assessment: Hotel Tax Rebate for other hotels

PwC estimates the potential cost of the Hotel Tax Rebate to be up to $23.8m (as shown in **Figure 7** on an NPV basis), when applied to the various hotel projects included in the DRCL Development Plan.

DRCL has presented the Hotel Tax Rebate as an important consideration in its decision to go forward with the hotel projects included in the DRCL Development Plan. However, PwC believes the following considerations must be taken into account when assessing the VfM provided to the CIG by the Hotel Tax Rebate:

- DRCL can also claim the Hotel Tax Rebate for any hotel it opens or renovates, including hotels it could build on properties outside of its land parcels adjacent to the WBR (for example at Camana Bay) or if it acquires an existing hotel and undertakes "renovations".
- The purpose of the Hotel Tax Rebate is to spur the development of new hotels or the renovation or refurbishment of existing hotels by DRCL. DRCL represented to PwC that it would not likely undertake hotel investment in the Cayman Islands as currently planned without the Hotel Tax Rebate. However, without a detailed analysis of projected ROI data on DRCL's proposed hotel developments it is not possible to establish the need for the Hotel Tax Rebate to make hotel investment financially feasible. Given that we have been informed that the DRCL Development plans are at an early stage, we understand that such analysis is not possible at present.
- Given the wide geographical scope and very long period during which the Hotel Tax Rebate is applicable, it is not possible for PwC to judge whether the Hotel Tax Rebate would have a significant impact on a hotel investment decision in the Cayman Islands nor what the likely impact on competitors' investment decisions would be.
- To PwC's knowledge, a similar rebate on hotel taxes has never been made available by CIG to a developer. Although CIG has in the past negotiated other incentives with hotel developers on a case by case basis, there is clearly a risk that the Hotel Tax Rebate could set a new precedent in the Cayman Islands, which would weaken CIG's negotiating position with alternative potential hotel investors.
- The potential cost of the Hotel Tax Rebate is highly subjective and very difficult to estimate given the possibility of the hotel tax rate increasing over time, which directly increases the value of the rebate. The recent decision by CIG to increase the hotel tax from 10% to 13% effectively increased the cost of the Hotel Tax Rebate to CIG by 30%.

Overall, PwC believes the Hotel Tax Rebate may not, as set out in the NRA Agreement, provide the CIG with VfM because:

- Except for the SMB Hotel, CIG does not know the size, type or location of any hotel developments which would be eligible for the rebate;
- The rebate could apply to existing hotels in which DRCL would acquire a 51% participation (or perhaps less); and
- Once the details of the Hotel Tax Rebate are made public, owners of existing hotels or other potential investors could make demands for similar rebates, at a cost unknown to CIG.

9.5. Overall assessment of NRA Agreement Value for Money

In summary, PwC believes that:

- The infrastructure and SMB Hotel development component of the NRA Agreements provides VfM to the CIG;
- In conjunction with the full or substantial delivery of the DRCL Development Plan, the $53m Abatements would provide VfM to the CIG, but improved targeting of incentives is required in order to avoid the risk of DRCL applying incentives to existing or planned developments which may be viable without tax waivers and/or to developments which might not have the tourism-related economic benefits which the CIG is seeking; and
- The Hotel Tax Rebate may not provide VfM to the CIG because CIG has little control over its application to either new hotels (of unknown category, size or location) or to existing hotels (without requiring substantial renovations) and because of the unknown impact it might have on other current or future hotel developers and owners.

9.6. CIG's alternatives to the NRA Agreement

The ETH Extension has been part of the Cayman Islands' infrastructure plans for over 20 years, with improved access and traffic flow to the West Bay population centre and the transfer of traffic volumes away from the WBR identified as being key infrastructure requirements. The NRA has confirmed that the WBR closure, while not part of their previous road planning, is consistent with the aim of 'pedestrianisation' of the WBR, leading to improvement in traffic safety and the general tourism offering in the Seven Mile Beach corridor.

PwC has examined the potential alternatives for delivery of the Road Infrastructure, by the 31 December 2013 deadline included in the Terms of Reference.

The Traditional Delivery method of NRA construction is dependent on the CIG financing the full cost of works. However, as discussed in Section 7, as a result of high existing debt levels and ongoing deficits, the CIG is required to carry out a significant fiscal retrenchment over the next three financial years. Given that there are a number of existing capital commitments on the Cayman Islands public purse, most notably the John Gray and Clifton Hunter High Schools, it is likely that any additional borrowing sanctioned by CIG and the FCO, would need to address these priorities. As such, in the circumstances, general prudent fiscal management as well as the provisions of the PMFL and the FFR would likely preclude raising new debt finance for Traditional Delivery of the road infrastructure by December 2013.

The option of CIG selling the WBR closure land to DRCL in a separate transaction and CIG building the ETH Extension itself was considered, given the potential benefits of improved transparency over WBR closure sale proceeds, greater control over development incentives and retention of control over the ETH Extension by the NRA. However, as outlined in Section 7.3.1, there are a number of disadvantages to this approach, and PwC concludes that the potential advantages can be achieved more effectively through amendment to the NRA Agreement.

Sale of alternative properties by the CIG to raise funds for the ETH Extension was considered, but in light of the significant synergy value released by the NRA Agreement, it seems unlikely that CIG would be able to secure proceeds on such terms for alternative public assets.

In light of CIG's fiscal constraints, PPP alternatives for provision of the ETH Extension are limited to those that would not require recognition of future obligations as public debt. Essentially, this limits PPP options to those that could operate as a stand-alone commercial enterprise, such as 'Real Tolling' or 'Tied-in Concessions'. Real Tolling for the ETH Extension is not considered commercially viable, given the expected traffic flow, investment required and feasible pricing. Tied-in Concessions would ordinarily comprise substantial transport infrastructure, such as airports and ports, or possibly sports stadia or casino concessions. Accordingly, there does not appear to be a realistic alternative option for a substantial Tied-in Concession along the route of the Road Infrastructure, particularly in light of DRCL's extensive adjacent land holdings.

9.7. Compliance with the FFR

The provisions of the NRA Agreement have the potential to generate substantial positive economic impact for the Cayman Islands and, as a result of the amendment and variance clauses in the NRA Agreement, the CIG has retained the ability to secure greater certainty over this economic benefit by further tailoring the tax waivers and abatements and other terms.

As such, and based on the likely impacts on public debt and revenues discussed in Section 8, the result of the NRA Agreement is expected to be compliant with the guidelines under the FFR and the CIG's five components of fiscal strategy.

In an assessment of compliance with the FFR, one must have regard to the appraisal and negotiation process undertaken by CIG, as well as the actual terms and expected outcomes of the NRA Agreement.

Ideally, and as set out under the FFR, this VfM review should have been conducted as part of the initial project appraisal at an early stage in the overall process, rather than at this late stage, and the CIG's own project appraisal should have been published for public consultation prior to the procurement stage. Further, PwC understands that in practice the NRA Agreement evaluation and negotiation was principally carried out by policy makers, as opposed to civil service ministries and departments.

However, the FFR was only signed in November 2011, toward the end of the NRA Agreement negotiation process. Further, while the FFR provides general guidance on approach, it seems that the PMFL's 2004 Regulations do not provide adequate detailed regulations for implementing the FFR's guidance around business appraisal, VfM review and negotiation for non-standard capital transactions with only one potential counterparty. As DRCL is the only counterparty which is able to generate the synergy value from the WBR closure, the NRA Agreement could not feasibly be put out to competitive tender, and is therefore not likely to be subject to CTC review, there does not appear to be a clear route for appraisal and project acceptance within CIG regulations. This is particularly the case given that the Public Sector Investment Committee envisaged under the PMFL has not been established.

It should also be noted that, by transferring the responsibility for the Road Infrastructure construction to DRCL, CIG is effectively putting the Road Infrastructure expenditure outside the scope of CTC's, and therefore the public's, review. This approach is standard practice for PPP arrangements internationally, in which Governments contract for the delivery of an 'outcome' and the means of delivery is essentially left to the private contractor, subject to provisions for proper identification, management and disclosure of potential or perceived conflicts of interest.

9.8. Recommendations

Based on its analysis and findings as documented in this report, PwC recommends the following modifications be made to the NRA Agreement to ensure it provides VfM to the CIG:

- If deemed appropriate from the perspective of developing the wider tourism industry, the Hotel Tax Rebate should be expanded to provide a CIG hotel tax rebate program available to all investors who undertake hotel construction or renovation projects on a scale comparable to the hotels envisaged in the DRCL Development Plan. Clear rules should be developed concerning eligibility of such projects for the hotel tax rebate, including a demonstration of the project's economic benefits for the Cayman Islands, scope and timing of the development.

- The stamp duty rebate provided to Caymanian purchasers of DRCL properties could potentially distort the local real estate market to the disadvantage of competing developers. As such, it is recommended that CIG consider whether any stamp duty concessions to Caymanians should be offered under a wider program, rather than one targeted solely at DRCL properties.

- CIG should establish a mechanism across its various departments and agencies to allow it to track all claims made by DRCL, its affiliates and sub-contractors under the $53m Abatements and the hotel tax rebate program to ensure claims made do not surpass the limits set out in the NRA Agreement and/or Hotel Tax Rebate program, and that waivers are awarded only for qualifying parties and qualifying development.

- CIG should consider amendments to the PMFL and associated Regulations in order to provide for a clear and transparent appraisal and approval process for non-standard transactions, such as the NRA Agreement, where competitive tender is not feasible. Such amendments should ensure that the process draws on a cross section of civil service expertise thereby enabling policy makers to focus solely on strategic policy.

- In light of the inherent reputational risk of CIG outsourcing major construction to a private developer, it is recommended that CIG provide DRCL with guidelines around identification, management and disclosure of any actual or perceived conflicts of interest in their procurement process. However, DRCL, as party responsible for road construction, would be expected to retain full discretion in its choice of suppliers and subcontractors.

- CIG could consider options to further incentivize and facilitate Caymanian employment in the new DRCL hotels. For example certain tax incentives, such as the Hotel Tax Rebate, could be linked to Caymanian employment metrics.

- DRCL will have complete control over the route and other aspects of the new pedestrian and bicycle path which will be the only means for public access to significant parts of West Bay Beach. This control is important for DRCL to be able to carry out its long term development plans. However, CIG should seek to enhance its control over this public amenity, without encroaching unduly on DRCL's need for commercial flexibility. A possible approach would be to oblige DRCL to consult with CIG before important changes could be made to the pedestrian and bicycle path, if appropriate this could be dealt with under a separate agreement or amendment to the NRA Agreement.

- The NRA Agreement foresees that development adjacent to the WBR Legal Closure shall be predominantly hotel/tourist resort-oriented. CIG should put in place a mechanism to ensure DRCL's WBR development respects these guidelines. Further, improved targeting of incentives is required in order to avoid the risk of DRCL applying incentives to existing or planned developments which may be viable without tax waivers and/or to developments which might not have the tourism-related economic benefits which the CIG is seeking. For example, a consultation process between CIG and DRCL should be required for major new developments to be subject to the incentives, in order that CIG can understand the wider impacts on the Cayman Islands economic and competitive environment and the expected level of inward investment generated. If necessary, this could be dealt with under a separate agreement or amendment to the NRA Agreement

- The Third Amendment includes provisions for when DRCL is assessed compensatory mitigation for sensitive habitat loss under a Coastal Works Licence or Coastal Works Permit. The impact of these provisions and the extent to which they modify CIG's standard approach in similar situations is not clear for PwC. CIG should have these provisions reviewed by legal counsel to fully assess their potential impact.

Appendix A. - Terms of Reference

Appendix B. - List of documents consulted

	Document
1	Caribbean tourism, local sourcing and enterprise development: review of the literature, Centre for Cultural Change, Sheffield Hallam University, Meyer (2006)
2	CIG Economic and Statistics Office, statistical compendiums 2006 - 2010
3	DRCL's Development Plan, preliminary estimates for real estate and tourism development alongside the WBR and ETH Extension over a period of over 25 years, April 2012
4	HM Treasury Green Book, Appraisal and Evaluation in Central Government 2011
5	HM Treasury, 2006, Value for Money Assessment Guidance,
6	Lodging Market Review Grand Cayman, prepared by REVPAR International for DRCL, December 21, 2011
7	National Audit Office, 2011 Analytical framework for assessing Value for Money
8	National Audit Office, 2011 Annual Report
9	PMFL Financial Regulations (2004)
10	Public Management and Finance Law (Revised)
11	Report on the For Cayman Investment Alliance (FCIA) Agreement, The Valuations & Estates Office, Lands and Survey Department, 9 November, 2011
12	Report on the For Cayman Investment Alliance (FCIA) Second Agreement, The Valuations & Estates Office, Lands and Survey Department, 2 October, 2012
13	Report on the Third Amendment to the Agreement between CIG/NRA & DRCL, The Valuations & Estates Office, Lands and Survey Department, 18 March, 2013
14	Time Series Analysis, Hamilton, J (1994)
15	The Cayman Islands' 2010 Census of Population & Housing Report
16	The direct and indirect Contributions of Tourism to Regional GDP: Hawaii, the Economic Research Organisation at the University of Hawaii Tian et al. (2011)
17	The Framework for Fiscal Responsibility agreed between the CIG and FCO on 23 November, 2011

List of documents consulted (Continued)

	Document
18	The NRA Agreement between CIG, NRA and DRCL, dated 15 December, 2011, which represents the subject of the VFM Review as well as the Second Amendment and the Third Amendment
19	The Roads Law (2005 Revision)
20	Tourist Accommodations (Taxation) Law
21	Traffic Impact Assessment of Proposed Esterley Tibbetts Highway Extension in Grand Cayman, Cayman Islands, report prepared for DECCO Ltd, Orth-Rodgers & Associates Inc, June 2011
22	Valuation and Analysis for Analysis of Proposed Roadway Changes, prepared by Andrews Key for DLS, September 23, 2011
23	Analysis of Proposed Roadway Changes Revision 1, prepared by Integra Realty Resources-Caribbean for DLS, 31 August, 2012
24	Analysis of Proposed Roadway Changes Revision 3, prepared by Integra Realty Resources-Caribbean for DLS, 25 February, 2013
25	Valuation: Land Used as Road re: West Bay Road Closing, prepared by Charterland Ltd for DRCL, 9 January, 2013
26	Report on review of Charterland Valuation on the Closure & vesting of West Bay Road (Part), prepared by DLS, 15 March, 2013
27	Valuation: Crown Lands Re: Proposed Closing & Vesting of West Bay Road, prepared by Charterland Ltd for DRCL, 12 December, 2012
28	Valuation Report: Land re. Barkers Road Closure, prepared by Charterlands Ltd. for DLS, September 29, 2011
29	Valuation Report: Land re. Barkers Road Closure, prepared by Charterlands Ltd. for DLS, February 20, 2013
30	Property Appraisal, Block 8A, Parcel 19 & 20 (part only), prepared by Bould Consulting Limited Ltd for DLS, 19 February, 2013
31	Valuation: Beachfront Land Re: Block 8A, Parcel 19 & 20 (Part), prepared by Charterland Ltd for DRCL, 5 November, 2012

32	Valuation of Undeveloped Land Block 13C Parcel 22, prepared by Bould Consulting for DLS, 22 August, 2012
33	Valuation of Undeveloped Land Block 4D Parcel 450, 293, 210 (part)22, prepared by JEC Property Consultants for DLS, August, 2012
34	Valuation Report of Land Parcels at Block & Parcels 4D106, 174, 210, 293 & 450, prepared by DDL Studio Ltd for DRCL, 13 October, 2011
35	Valuation of Land at Block 7C Parcel 70, prepared by Blue Point Consultants Ltd for DLS, 10 December, 2012
36	Valuation: Development Site Re: Land on South Church Street; Block 7C Parcel 70, prepared by Charterland Ltd for DRCL, 16 July, 2012
37	Valuation Report: Land Re: Proposed West Bay Community Park, prepared by Charterland Ltd for DRCL, 20 September, 2011
38	Valuation of Land at Block 13C Parcel 22 (part), prepared by Blue Point Consultants Ltd for DRCL, 24 January, 2013

Appendix C. - Term Sheet Summary of NRA Agreement

NRA Agreement ("Agreement") Summary of Key Terms[53]

DRAFT
Reflecting Third Amendment, April 12, 2013 version
May 8, 2013

Clause	Description
Benefits to be provided by DRCL to CIG/NRA	
1 + 70 + 72 8 38 35 54	Construction of ETH Extension, including the possible construction of the ETHR2 Roundabouts, from Raleigh Quay to Batabano Road and the Reverend Blackman Drive Extension from the ETH to Willie Farrington Road (as set out on page 1 of 16 of the schedules to the Agreement). Design and construction quality must be consistent with: ➢ Design and quality of ETH as constructed between Gecko Link/Galleria Loop and Raleigh Quay ➢ AASHTO's Policy on Geometric Design of Highways and Streets ➢ For highway structures, Florida Department of Transportation's Structures Manual Design of ETH Extension is subject to NRA approval DRCL may seek certification of Completion of proposed Road Works by the Engineer of Record if: ➢ NRA does not act within 14 days of a request by DRCL; or ➢ DRCL is not satisfied with the NRA's decision
3 + 4 +13	DRCL responsible for the design and construction, at its sole cost and expense, of the road works described in 4.1 to 4.6, including any compensation CIG is required to pay
Third Amendment, 1 to 5	Funding by DRCL of the budget of cost of Construction of the ETH Expansion by the NRA, that is transforming it from a two lane road to a four lane divided arterial road, from the Bank of Butterfield Roundabout (BOBR) to the Lawrence Boulevard Roundabout (LTBR1) ➢ NRA is responsible for any actual costs which exceed the budget of costs
Third Amendment, 6 to 9	DRCL to construct, at its sole cost and on the NRA's behalf, the ETH Expansion between LTBR1 and Limestone Roundabout (LSR) ➢ DRCL to complete Construction to coincide with the end of the NRA's construction of the ETH Expansion between BOBR and LTBR1
Third Amendment, 14	CIG shall be responsible for all costs relating to lighting and for all obligations of CUC in relation to the ETH Expansion.
Third Amendment, 15	Any difference, whether positive/negative, between the agreed costs of the ETH Expansion and US$11m will be added/subtracted to to the NPV Sum of Part 1 of the Investment and Development Incentives Schedule.
12 + 71 + Third Amendment, 12 + 25	DRCL to transfer to CIG ownership of any land required for the ETH Extension (approximately 32.94 acres) and the Reverend Blackman Drive Extension as well as in respect of the ETH Expansion(only applies to new public road declarations relating to ETH Expansion, that is no claims for existing gazetted ETH) and the Sunrise Adult Training Centre public road access. DRCL irrevocably waives any associated compensation.

[53] This summary set out the most important business issues included in the Agreement, the Second Amendment ant the Third Amendment (draft version prepared on April 12, 2013). It is not a summary of all aspects of the Agreement and subsequent amendments, in particular of its administrative clauses and general conditions. The reader should refer to the complete Agreement, including the Second Amendment and the Third Amendment, in order to have a complete understanding of all of its aspects.

Clause	Description
Benefits to be provided by DRCL to CIG/NRA	
13 + Third Amendment, 12 + 25	DRCL shall reimburse CIG for the full amount of any compensation CIG is required to pay in respect of the Construction of the ETH Extension as well as in respect of the ETH Expansion (only applies to new public road declarations) and the Sunrise Adult Training Centre public road access.
39	DRCL agrees to whenever possible procure the provision of labour and or materials and/or works from a broad cross-section of qualified and competent Caymanians or Caymanian owned firms.
44 + Third Amendment, 13	DRCL rights to install "conduits… under or across the ETH or any other road Constructed in connection with this Agreement" covers only the new extension of ETH, Barkers and ACR as well as the ETH Expansion.
47	DRCL to cover costs of moving CUC power lines from area of West by Road Legal Closure. Although the NRA Agreement declares that Government is not responsible for cost, DRCL has anticipated paying CUC for this.
65	Should DRCL construct a roundabout at West Bay Road and Camana Way, DRCL will transfer to CIG the ownership of land required for the roundabout. DRCL irrevocably waives any right to any associated compensation.
69	Should NRA construct a roundabout at ETH and Batabano Road, DRCL will transfer to CIG the ownership of land required for the roundabout. DRCL irrevocably waives any right to any associated compensation.
6 +12 + 15	DRCL waiver of compensation under the Roads Law, for land required in respect of the ACR, providing the road declaration is made within 4 years and in accordance with design and alignment satisfactory to DRCL. DRCL waiver of compensation (if any due after allowing for betterment) for the ETH works, DRCL indemnification of NRA to cover any third party compensation claims on ETH. See clauses 12 to 15.
Third Amendment, 16	CIG/NRA approve, at DRCL's option, either one roundabout or one full road access approximately 2,800 feet south of ACRR2, provided that DRCL reimburse CIG for all of its costs related to acquiring any needed land.
114 + 115	Funding of US$5M paid to CIG upon execution of the Agreement, for educational, community and training programs
119	DRCL to reopen SMB Hotel, starting construction work with 12 months of the date of the Agreement, and continuing construction until the SMB hotel is reopened.
Second Amendment, 4 + 6 + 12 + 13 Third Amendment, 31	DRCL to develop the Public Beach Park and New Public Beach provided the costs and expenses to complete such development shall not in any event exceed US$3M, completing development within nine months of CIG undertakings set out in clauses 6.2.1 and 6.2.2.
Second Amendment, 16 Third Amendment, 40 + 41	Should DRCL receive permission to develop its land in Barkers from the Central Planning Authority, it can require CIG and the NRA to have the existing public roads in Barkers Legally Closed or realigned to facilitate DRCL's development.
Second Amendment, 17 + 19	DRCL shall transfer to CIG, for nil consideration, three acres of land (of which two are filled to 4' above sea level) west of the ETH near Camana Bay for the purposes of a new Sunrise Adult Training Centre.
Third Amendment, 23	DRCL shall fund the NRA's budget of actual costs of the construction of a public road access between the ETH and the Sunrise Adult Training Centre.
Second	DRCL to provide pedestrian and bicycle paths for use by the public in perpetuity as set out for

Clause	Description
Benefits to be provided by DRCL to CIG/NRA	
Amendment, 20 Third Amendment, 26	illustrative purposes on the West Bay Road and ETH Extension Plan– Proposed Pedestrian & Bicycle Paths For that area from and including the Public Beach Park to Raleigh Quay, DRCL undertakes to locate all pedestrian and bicycle paths it provides on its land west of all major structures and buildings and no more than 200 feet from the mean high water mark.
Second Amendment, 21 Third Amendment, 37 + 38	DRCL shall transfer to CIG, for nil consideration, 20 acres of land within the West Bay Properties of which: ➢ 15 acres are for educational and community purposes; and ➢ 5 acres are for the purpose of a new cemetery.
Third Amendment, 29	CIG shall make a Public Road Declaration in respect of the New Public Beach Road which will provide access to the Public Beach Park as well as to DRCL's Calico Jack's restaurant
Third Amendment, 17	DRCL shall, for nil consideration, surrender its leasehold interest in the Soto Land, upon the completion of WBR Legal Closure & Raleigh Quay Legal Closure.
Third Amendment, 19	DRCL shall transfer to CIG the New Public Beach at Barkers in return for CIG: ➢ Completing the West Bay Road Legal Closure and the Raleigh Quay Legal Closure; ➢ Relocate the two existing public rights of way registered over Parcels 11B/61 and 11B/83 to: • The northerly most 12 feet of Parcel 10E/53; and • Part of the southerly most 12 feet of Parcel 11B/70 ➢ Passing legislation providing for the transfer of beach lands in lieu of the requirement for setting aside and dedication public rights of way to the sea
Third Amendment, 21	DRCL shall transfer to CIG, for nil consideration, Smith's Cove in return for CIG: ➢ Completing the West Bay Road Legal Closure and the Raleigh Quay Legal Closure; ➢ Relocate the two existing public rights of way registered over Parcels 11B/61 and 11B/83 to: • The northerly most 12 feet of Parcel 10E/53; and • Part of the southerly most 12 feet of Parcel 11B/70 ➢ Passing legislation providing for the transfer of beach lands in lieu of the requirement for setting aside and dedication public rights of way to the sea
Second Amendment, 16 Third Amendment, 40 + 41	Following the legal closure of public roads in Barkers at DRCL's request, DRCL shall accommodate and assist with providing public access to the Barkers National Park. DRCL shall not claim compensation for land required for the New Barkers Road and shall fund the NRA's cost of the Construction of the road. If required, this will include the Construction by the NRA of a New Barkers Road which will be funded by DRCL.

Clause	Description
Benefits to be provided by CIG/NRA to DRCL	
5 + 9 + 191 + 27.2 + Second Amendment, 2	Portions of West Bay Road and Raleigh Quay (as set out on pages 2 to 4 of 16 of the schedules to the Agreement as revised in Second Amendment) to be legally closed by CIG and vested in adjacent property owners (for nil consideration), any related Stamp Duty waived by CIG.
17	CIG and NRA responsible for lighting on ETH Extension, at a standard equivalent to that on the ETH between Gecko Link/Galleria Loop and Raleigh Quay
20-25, 26 Third Amendment, 13	Exclusive licence for 99 years for DRCL to place its commercial signage on or adjacent to the ETH Extension, the ETH Expansion and those portions of the ETH which pass through or are approximate to land owned by DRCL. CIG will place signage to Camana Bay and other DRCL developments on other roads not subject to this licence.
44 + 48 Third Amendment, 13	DRCL to have right to install conduits under the ETH Extension, the ETH Expansion, Raleigh Quay, Governor's way, Reverend Blackman Drive Extension and any part of the ETH which it Constructs, and be entitled to licence for a fee such conduits to any utility provider. Utility providers other than CUC, Water Company and Water Authority shall be required to use such DRCL conduits in the event they need to install services along the ETH.
61	DRCL may construct, at its expense, a pedestrian crossing at ETH and Camana Way
63	DRCL may construct, at its expense, a pedestrian crossing at West Bay Road and Camana Way
64	DRCL may construct, at its expense, a roundabout at West Bay Road and Camana Way
72	DRCL may construct, at its expense, two roundabouts between ETHR1 and ETHR3
75	Approval by CIG and NRA of a Full Road Access and two left in left out accesses on the ACR between ACRR1 and ACRR2
80 + 81	DRCL may construct, at its expense, pedestrian bridges across the ETH between the SMB Hotel and Batanabo Road. CIG grants DRCL an easement in relation to any such bridge.
82	NRA responsible for all ongoing maintenance for any roads or similar works constructed under the Agreement except for pedestrian bridges constructed by DRCL
87	A waiver of 100% of all Import Duties on materials, goods and equipment imported by DRCL or its Affiliates, contractors and sub-contractors in relation to the Proposed Road Works and any Construction of Public Infrastructure directly related to the Proposed Road Work
89 Third Amendment, Investment and Development Incentives Schedule, Part I	Concessions, waivers and abatements as set out in the "Investment and Development Incentives Schedule" of the Third Amendment, including: ➢ Up to an NPV amount (calculated using a 10% discount rate) of US$52.95m: • 100% waiver of Development Fees and Import Duties for all DRCL properties (including affiliates' properties) • 100% waiver of DRCL Related Stamp Duty • 50% waiver of stamp duty payable in respect of all leases in the West Bay Properties • 50% rebate of all taxes levied pursuant to the Tourist Accommodation (Taxation) Law for the SMB Hotel for a period of 10 years after it is opened ➢ Development adjacent to the West Bay Road Legal Closure will be predominantly hotel/tourist resort-oriented, along with ancillary projects such as condominiums, associated real estate and other amenities
Third Amendment, Investment and Development Incentives Schedule,	➢ 50% rebate, for 10 years, of all taxes levied pursuant to the Tourist Accommodation (Taxation) Law for all hotels opened, reopened, renovated or refurbished by DRCL during the 30 years from the date of the Agreement • A single hotel can be subject to this rebate only once, including its initial construction • The refurbishment/renovation must represent an investment of a minimum of the lesser of

Clause	Description
Benefits to be provided by CIG/NRA to DRCL	
Part II	– US$50,000 multiplied by the number of hotel rooms in the hotel; or – 15% of the hotel's fair market value at the time • These expenditures must be incurred over a period of no more than 24 months ➢ For 30 years from date of the Agreement: • Stamp duty payable by Caymanian purchasers of residential and commercial property in Camana Bay and the West Bay Properties shall be the lesser of 50% of the applicable duty or 4%; and • 100% rebate on all Development Fees and Import Duties in relation to construction of Public Infrastructure by DRCL, its contractors or sub-contractors
144 + 146	CIG and NRA to give priority to all DRCL matters relating to the Agreement
Second Amendment, 8	CIG will be solely responsible for the maintenance of the Public Beach Park and New Public Beach
Second Amendment, 10	DRCL no longer required to provide any other rights of way from a public road, or otherwise, to the sea in respect of any development of Parcels 10E/62, 10E/53, 10E/54 as well as the land between and including the southern boundary of Parcel 11B/70 to the northern boundary of Parcel 10E/10
Second Amendment, 16	Upon Central Planning Authority approval of DRCL's application to develop any part of the Barkers DRCL Land, CIG shall take all steps required to have all public roads in Barkers legally closed and/or realigned to facilitate the development of the Barkers DRCL Land
Third Amendment, 19	The two existing public rights of way registered over Parcels 11B/61 and 11B/83 at the SMB Hotel to be consolidated and relocated to: ➢ the northerly most 12 feet of Parcel 10E/53; and ➢ Part of the southerly most 12 feet of Parcel 11b/70.
Third Amendment, 20	CIG to pass legislation providing for the transfer of lands, in the same district and of equivalent value, for the purpose of public beach facilities in lieu of the requirement for setting aside and dedicating public rights of way to the sea (either for new development or for existing public rights of way).
Third Amendment, 32	Pending the completion of the transfer of DRCL's leasehold interest in the Soto Land, CIG will indemnify DRCL for any costs or liabilities incurred resulting from the use or occupation by third parties of the Soto Land.
Third Amendment, 47	In respect of Coastal Works Licence or Coastal Works Permit where compensatory mitigation for sensitive habitat loss is applicable, DRCL shall be entitled, as agreed with CIG, to either: ➢ transfer and vest absolutely in CIG environmentally sensitive lands ➢ pay an amount in respect of compensatory mitigation; or ➢ transfer land and pay an amount, provided any land transferred shall not be subject to Public Open Space zoning or similar restrictions.

Appendix D. - NRA Agreement

Appendix E. - JEC report

Appendix F. - Schedule 1, Specific CIG Needs and Benefits

The CIG has identified the following needs:

- Economic Needs
  - Create a vibrant and sustainable economy;
  - Create employment and other opportunities for Caymanians, including the creation of new jobs in the construction and associated industries;
  - Stimulate economic activity within the immediate short-term (within calendar year 2012); and
  - Stimulate projects which will create long-term annual revenues for the CIG.
- Infrastructure Needs
  - To make needed improvements to the Cayman Islands' roads infrastructure, to improve traffic flow and emergency service access to communities, and provide secure alternative traffic routes; and
  - Enhance and develop high end tourism facilities and product.
- Social Needs
  - Positively impact the quality and availability of education and training for Caymanians; and
  - Enhance and deliver community and social programs.

Aligned with these needs, the specific benefits that will be delivered by the Agreement are:

- Socio-Economic Benefits
  - A positive increase to the Cayman Islands GDP over 2010 levels, including both direct and indirect economic activity;
  - An increase of jobs during road construction and hotel redevelopment and the operation of the redeveloped hotel, including both direct and indirect employment;
  - Revenues to CIG through indirect economic activity, as a result of the economic multiplier of the direct spend;
  - A residential mortgage arrears assistance program available to qualified Caymanians in the sum of $2.5 million; and
  - Education, parks and housing in the sum of $2.5 million.
- Infrastructure Benefits
  - The following road infrastructure projects valued at approximately $35 Million to be completed by December 2013:
    - The extension of the Esterley Tibbetts Highway to Batabano Road;
    - The construction of Reverend Blackman Road west of the Esterley Tibbetts Highway to
    - Willie Farrington Drive; and
    - Construction of the Barkers Road.
  - Enhancement of the high-end physical tourism infrastructure and product through the redeveloped SMB Hotel.
- Strategic Alignment

  In addition to the specific needs and benefits outlined above, the CIG believes the NRA Agreement aligns with the CIG's broad goals and key policy strategies, as defined in the CIG's 2012/2013 Strategic Policy Statement ("SPS") including:
  - Strengthening our Infrastructure
    - Continued upgrading and development of the road network.
    - Extension of the Esterley Tibbetts Highway.
  - Preserving our Culture

- Continue the development of Barkers National Park.

– Restoring Prudent Fiscal Management

- Use of Private Finance Initiatives (PFI) and Public-Private Partnerships (PPP) as alternatives for funding/developing large public sector capital projects.
- Limit borrowings to absolute minimal levels to maintain the high Sovereign rating, fiscal sustainability and international reputation.
- Operate within the new Framework for Fiscal Responsibility.