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Lansdowne Partnership Plan Financial Update

24 September 2012

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Notice to Reader

PricewaterhouseCoopers LLP ("PwC") has provided advisory services to Graham Bird and Associates ("Client") in regards to the City of Ottawa's (the "City") Lansdowne Redevelopment Project. Our Services were performed and this Report was developed in accordance with our engagement letter dated 1 February 2010 and are subject to the terms and conditions included therein. This report contains confidential and competitive information, the release of which would be harmful to the City, the Client and to PwC. This report, or portions thereof, should not be referred to or distributed orally or in writing, to any other persons or entity other than the City or the Client, without PwC's written consent.

Our work, and the financial forecasts presented herein, are based primarily on information supplied by the City's project team, including external advisors and was based only on the information made available from 9 Feb 2012 to 5 September 2012. Our work was limited to the specific procedures and analysis described herein. It was carried out on the basis that such information is accurate and complete. Information was not subject to checking or verification procedures, except to the extent expressly stated to form part of this scope of our work. Actual results may vary from those presented and the variations may be material. No assurances are provided that the results indicated in the various analysis discussed in this report will be borne in practice. These forecasts may change based on additional analysis and data.

Our work did not constitute an audit conducted in accordance with generally accepted auditing standards, an examination of internal controls or other attestation or review services in accordance with the standards established by the Canadian Institute of Chartered Accountants (CICA). Accordingly, we do not express an opinion or any other form of assurance on the financial or other information, or operating and internal controls of the project.The reader agrees that PricewaterhouseCoopers LLP, its partners, employees and agents neither owe nor accept any duty or responsibility to it, whether in contract or in tort (including without limitation, negligence and breach of statutory duty), except to the Client under the relevant terms of the engagement, and shall not be liable in respect of any loss, damage or expense of whatsoever nature is caused by any use the reader may choose to make of this report, or which is otherwise consequent upon the gaining of access to the report by the reader.

Table of Contents

1. Introduction

The Lansdowne Partnership Plan ("LPP" or the "Plan") includes development of the stadium, arena and associated parking (the "Stadium"), retail and associated parking ("the Retail"), the Office development ("the Office") and residential tower and town homes ("the Residential Development"), all located on the existing Lansdowne site. The Plan is based on a proposed business transaction between the City and Ottawa Sports and Entertainment Group ("OSEG")[1] for the revitalization of Lansdowne Park which includes contributions from both parties to select components of the Plan. In addition to the core transaction with OSEG, the City has plans to rehabilitate the urban park that adjoins the Stadium.

The LPP is based on a 'closed financial system' that captures capital costs and contributions which have been agreed upon by both partners, and cash-flows from operations to provide the basis for future distributions to the City and to OSEG. It is important to note that the closed financial system includes some, but not all of the physical components of the Lansdowne redevelopment[2].

The purpose of this financial update is to i) provide a summary description of the structure of the agreement between OSEG and the City included in the closed financial system, ii) provide an updated pro forma including a review of important changes in assumptions from February 2012 to present and their impact on the expected returns to the City and OSEG, and iii) a summary of the extent to which the City's contribution is revenue neutral relative to its expected returns and avoided costs.

PwC was retained by Graham Bird and Associates, to develop a financial pro forma for the City of Ottawa on the Lansdowne project covering the period from 2012 to 2044 and to provide ad-hoc financial advisory support. The City's assumptions included inflation, financing costs, taxes, capital costs, infrastructure and parking costs for residential and Office forecasts, and air rights. OSEG's assumptions included estimates for the operating revenues and expenses for each component, capital costs, financing costs, and equity contributions.

This report covers the period from 9 February 2012 to 24 September 2012. PwC has reviewed those assumptions that have changed from February 2012 and that have had a significant impact on the final pro forma. These include:

- the City's maximum capital cost resulting from the tender of the Stadium;
- the operating and financial elements of the Retail development; and
- the City's lifecycle reserve.

OSEG has amended other assumptions which are incorporated within the pro forma, however, these are outside of the scope of our review.

2. Structure of the Agreement between OSEG and the City

The legal structure proposed for the LPP contains a number of partnerships (limited and general), and the use of special purpose vehicles, which serve to limit each party's exposure to specific LPP components. The legal structure

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[1] OSEG Members comprise Lansgreen Investments Inc., Shenkman Lansdowne Ltd., Trinity Lansdowne Ltd., Keljay Ltd. and Friarmere Holdings Inc.

[2] See appendix A for more detail on the closed financial system.

provides for a Master Limited Partnership (MLP). Set out below are two important points to note about the Master Limited Partnership:

- Net cash flow of the closed system is consolidated in the MLP. To the extent that one component partnership experiences negative annual cash flow, the MLP will be required to make the required contributions to annual operating requirements; and

- While OSEG and the City have equal interests in the MLP, their respective returns from the partnership are provided through the waterfall distribution structure, as described in section 2.3.

2.1 Roles and Responsibilities

The aforementioned partnerships and accompanying commercial terms are set out in a series of legal agreements[3], including the Project Agreement, which identifies broad roles and responsibilities for each of the City and OSEG, as follows:

- **The City**: as a partner in the LPP, the City will contribute funds to rehabilitate the Stadium and the land on which the Retail, Residential Development and Office components reside. As landlord, the City will hold the leases for the use of the renovated Stadium and the use of the Retail and Office lands.

- **OSEG**: as a partner in the LPP, OSEG will contribute the required Minimum Equity and Additional Equity to construct the Retail development, acquire the professional sports teams and fund operating losses through to completion. OSEG will contribute Additional Equity or Stadium Completion Funds to fund negative cash flow through both the construction and the operating periods. In addition, OSEG will serve as development manager for the reconstruction of the Stadium and the Retail development. OSEG will also be responsible for sub-leasing the Retail facilities and the Office developer will be responsible for sub-leasing the Office space to tenants. Finally, OSEG will be responsible for the operations and maintenance of the Stadium and Retail components (including the mixed use area).

2.2 Construction Risk

The City has taken a number of steps to mitigate its exposure to risks that could arise from the LPP. On financial close, OSEG will provide the City with a committed maximum cost for the redevelopment of the Stadium. OSEG will hold the contract with the general contractor for the redevelopment and, to the extent that additional funds are required to complete the project, OSEG is to provide these as Stadium Completion Funds. OSEG is then able to recover any Stadium Completion Funds contributed, along with an 8% annual return while invested, from the closed system waterfall as described below.

We understand that OSEG will be seeking a fixed price contract with a general contractor for the redevelopment of the Stadium. At the time this report was issued, the contract was still under development, and as such, we have not been able to review the underlying allocation of risk between OSEG and the general contractor. It is important to note that while OSEG is responsible for providing additional funds to complete the Stadium, the return on these funds ranks above the City's returns on Deemed Equity.

[3] See: Description of and Material Business Terms for Lansdowne Partnership Plan Legal Agreements, September 2012.

2.3 Waterfall Distribution Structure

The MLP has defined a basis for distributing free cash flow to the City and to OSEG which are ranked at six levels, with distributions at each level undertaken on a pari passu basis. The relative priorities set out in the waterfall structure are the product of extensive negotiations between the City and OSEG, and represent a balance between contributions made to the Lansdowne project and responsibilities assumed.

- L1: Additions to Lifecycle Fund – annual contributions to the lifecycle fund are made prior to cash distributions at other levels. This fund is required for the upkeep and maintenance of the Stadium.
- L2: Return on Equity – the City of Ottawa and OSEG are entitled to a return on their respective equity contributions. To the extent that there is insufficient net cash flow to fully fund the current year and previous years' accumulated deficiencies, payments will be made to each party proportionate to what they are owed at this level in total.
    a. The City is entitled to an 8% return per annum (cumulative but not compounding) on its outstanding City Funding Equity.
    b. OSEG is entitled to an 8% return per annum (cumulative but not compounding) on its outstanding Equity (sum of its outstanding Minimum Equity, Stadium Completion Funds and Additional Equity accounts).
- L3: Return of Additional Equity – OSEG is entitled to receive any additional equity contributed back on an unamortized basis.
- L4: Return of Equity and Stadium Completion Funds – the City and OSEG are entitled to repatriate their equity. To the extent that there is insufficient net cash flow to fully fund the current year and previous years' accumulated deficiencies, payments will be made to each party proportionate to what they are owed at this level in total.
    a. The City is entitled to have its Funding Equity returned, amortized straight-line over 27 years beginning after the third year of operations.
    b. OSEG is entitled to have its Minimum Equity and Stadium Completion Funds returned, amortized straight-line over 27 years beginning after the third year of operations.
- L5: Return on Deemed Equity – City is entitled to an 8% return per annum (cumulative but not compounding) on the fair market value of the retail and Office land.
- L6: Cash share – to the extent that all previous levels are current and there exists additional net cash flow, the City and OSEG will share any remaining amounts equally.

3. Financial Pro Forma Update

The LPP has advanced in design, planning and development since February 2012. The City has refined estimates for its interest rate on the long term debt. OSEG has refined its estimates through input provided by new expert advisors, data from comparable facilities in Canada, tenders for construction works and the finalized legal agreements.

The table below summarizes the revenues (sources), expenses (uses) and net cash flow for each of the components in the closed financial system and the changes to those variables between February 2012 and September 2012. The variations are then explained in the sections below.

(in $ millions)	Sep-12	Feb-12	Change ($)	Change (%)
Revenue				
Stadium and Arena	158.4	154.8	3.6	2%
Naming Rights	50.2	15.7	34.5	219%
CFL	775.7	727.8	47.8	7%
OHL	154.6	149.0	5.6	4%
Parking	87.0	82.9	4.2	5%
Retail	189.3	222.5	(33.2)	-15%
Total Revenue	1415.2	1352.7	62.5	5%
Expenses				
Stadium and Arena	(170.7)	(167.4)	(3.2)	2%
Naming Rights	(1.2)		(1.2)	
CFL	(731.9)	(688.3)	(43.6)	6%
OHL	(147.1)	(138.2)	(8.9)	6%
Parking	(49.9)	(51.2)	1.3	-2%
Total Expenses	(1100.8)	(1045.1)	(55.7)	5%

(in $ millions)	Sep-12	Feb-12	Change ($)	Change (%)
Net cashflow				
Stadium and Arena	(12.3)	(12.6)	.3	3%
Naming Rights	49.1	15.7	33.3	212%
CFL	43.7	39.5	4.2	11%
OHL	7.5	10.8	(3.3)	-31%
Parking	37.1	31.7	5.4	17%
Retail	189.3	222.5	(33.2)	-15%
Total	314.4	307.6	6.8	2%

Retail Revenue includes the financing activities, expenses and debt servicing

The changes to the pro forma above are often the result of one or more factors that could affect multiple components in the LPP. As a result, it is not possible to attribute a single cause for each particular change. However, we have reviewed the factors that have had the most significant impact on the financial projections and have summarized these below.

3.1 Project Timing

In all previous iterations of the Lansdowne pro forma presented to Council it was assumed that the LPP structure and waterfall provisions would cover the thirty year period from January 1, 2014, the anticipated completion date to December 31, 2043. With the recent change in the schedule, the anticipated completion date is changed to May 1, 2014. The legal agreements have since been revised such that the waterfall will now expire 31 December 2044 regardless of the operational term of the components. In addition, the construction schedule for the Stadium and Retail has been revised such that these components are now expected to be open at different dates in 2014. This shift in the operating term from February 2012 has had two principal effects on the pro forma:

- Inflation: in all instances nominal revenues and costs have been adjusted to account for the delay in opening, which has increased both revenues and costs over the analysis period.

- Increased term: in some cases the components will be operational for a longer period of time, due to the inclusion of a partial year's operations.

3.2 The Stadium and Arena

The total estimated construction cost for the Stadium has increased to $135.8 million from $129.3 million. Operating revenues have increased by 2% to $158.4 million and operating expenses have increased by 2% to $170.7 million. There is approximately $0.3 million increase in net cash flow to the waterfall from the Stadium relative to what was presented in February 2012. Factors that contributed to the change in net cash flow to the waterfall are summarized below.

- The operating term for the financial pro forma is extended till 31 December 2044. This change has increased the operating revenues and expenses.
- Concession revenues during the regular season for the professional sports teams have decreased.

Total nominal contributions to the City's lifecycle reserve for the Stadium have increased to $58.5 million from $58.4 million in February 2012[4]. The lifecycle cost is revised due to a third party report and amended term of the lifecycle contribution which now covers the period from 1 January 2015 to 31 December 2044.

3.2.1 Naming Rights

Revenues received from the assignment of naming rights have increased from $15.7 million in February 2012 to $50.2 million, based on comparable facilities and agreements in Canada, and the guidance provided by OSEG's consultant. Approximately $1.2 million in overhead expenses have now been attributed to this component. Total cash flow from Naming Rights is approximately $49.1 million in net cash flow to the waterfall over the operating term. This represents a $33.3 million increase from the previous estimate that was presented in February 2012.

3.2.2 The CFL Team

Revenues have increased by 7% to $775.7 million and the corresponding expenses have increased by 6% to $731.9 million. These changes represent an increase of approximately $4.2 million in net cash flow to the waterfall over the operating term relative to the February 2012 estimate. Factors that contributed to the change in net cash flow to the waterfall are summarized below.

- The operating term for the financial pro forma is extended to 31 December 2044. This change has increased the operating revenues and expenses.
- Half of the athletic therapy costs are now allocated to the professional soccer team. This change has decreased expenses and increased net cash flow.
- Following a review of the CFL business summary, OSEG has increased pre-season concession revenues.
- The Stadium is now expected to house a small amount of retail space for a team store that will carry souvenirs and memorabilia. The CFL team will operate the store and pay a rent to the Stadium limited partnership. This change has increased the team's operating expenses.
- Start up costs related to the acquisition of equipment has increased.
- Additional seats will be available due to a design change in the Stadium. This has increased the revenues for the CFL.

[4] As noted previously, contributions to the City's lifecycle reserve are the first level of distributions in the waterfall and not an expense to the Stadium Limited Partnership.

3.2.3 The OHL Team

Revenues have increased by 4% to $154.6 million and the corresponding expenses have increased by 6% to $147.1 million. The OHL component is contributing $3.3 million less in net cash flow to the waterfall over the operating term as compared to what was presented in February 2012 estimate. Factors that contributed to the change in net cash flow to the waterfall are summarized below.

- The operating term for the financial pro forma is extended till 31 December 2044. This change has increased the operating revenues and expenses.
- Operating losses are anticipated during the 2012/13 and 2013/14 seasons when the team will be temporarily relocated to the Scotiabank Place. Allowance for these losses has increased the operating expenses.

3.3 The Parking Component

Parking revenues have increased by 5% to $87.0 million and the corresponding expenses (including lifecycle) have reduced by 2% to $49.9 million. The parking component is contributing approximately $5.4 million more in net cash flow to the waterfall relative to what was presented in February 2012. The change in operating revenues and expenses can be attributed to following items:

- The operating term for the financial pro forma is extended till 31 December 2044. This change has increased the operating revenues and expenses.
- The Office owner has been allocated a share of operating revenues (pro rata to the number of stalls it holds). This change has reduced the operating revenues included in the closed system.
- The Office and residential owners have been allocated a share of operating expenses (pro rata to the number of stalls they hold). This change has reduced the operating expenses.
- Revenues associated with special programming on the urban park have increased.

The Retail component's share of the lifecycle costs for parking has increased to $8.4 million from $6.3 million. This change is primarily due to an increase in the estimated costs of construction and the revised lifecycle contribution period from 1 January 2015 to 31 December 2044.

3.4 The Retail Development

The Retail development continues to be sized at approximately 360,000 square feet of leasable space, with a requirement to build 360 parking stalls, fund infrastructure, common space and to contribute $2.5 million to the urban park budget. The construction cost for the Retail (including parking) has increased to $ 126.6 million from $116.2 million. The net cash flow to the waterfall has decreased by $33.2 million relative to the February 2012 estimate. Several assumptions have affected the cash flow from Retail operations:

- Gross revenues from tenant rents have decreased from $468.0 million to $417.2 million. This change has reduced net cash flow to the waterfall by approximately 50.8 million; however this decrease has been partially offset by further changes to the retail pro forma as described below.
- The operating term for the financial pro forma is extended till 31 December 2044. This change has increased the operating revenues and expenses.
- The vacancy rate profile for the Retail development has been amended in two ways. First, the steady state, or stabilised vacancy rate for the development has been reduced from 5% to 3% and OSEG has included a stabilisation period through which vacancies fall from 5% in the first two years of operations, to 4% in the third and fourth years, and finally stabilising at 3% in year 5. The revised vacancy profile increased cash from tenants, and has decreased the net tax cost of vacancies to the closed system. It has been assumed that the permanent financing will be lent on the basis of the stabilised vacancy rate.

- In July 2012 OSEG commissioned the Altus Group to update their 2009 study on the pro forma realty taxes that would be generated by the current (and anticipated) mix of Retail and Office space. This study identified an increase relative to the February 2012 pro forma estimate. While not included in the closed financial system, this increase affects the relative share of realty taxes required to cover the City's debt charges net of avoided costs and waterfall distributions, as described in section 4 below.

3.4.1 Financing Assumptions

We understand that OSEG has sought feedback from banks on the underlying financing assumptions for both the construction financing used to fund the Retail development construction, and the permanent financing that will be secured against the Retail development. That feedback has led to some changes in the financing assumptions as described below.

3.4.1.1 Construction Financing

Changes in the construction financing are presented below:

- Annual interest rate for construction financing is revised to 4.25% from 4.50% to reflect the current market rates.
- An additional 0.60% Minto fee is applied on construction financing. This fee is payable by the Retail Limited Partnership.
- Loan to costs ratio on construction financing has increased from 65% to 75%.

3.4.1.2 Permanent Financing

Changes in the permanent financing are summarized below:

- Annual interest rate for the permanent financing is reduced to 5.48% from 5.98% to reflect the current market rates.
- An additional 0.25% Minto fee is applied on permanent financing. This fee is payable by the Retail Limited Partnership.
- The amortization period on the Retail mortgage is increased to 30 years from 25 years.
- Loan to value on the Retail mortgage has increased from 65% to 70% of estimated value of the Retail. This has increased the maximum size of the Retail mortgage.
- Capital repairs on the Retail development were previously funded through the issuance of a second mortgage in the 26th year of operations. Currently, repairs are assumed to be funded throughout the life of the project with free cash flow both from the closed system and from tenant recoveries

3.5 Overhead Expenses

In addition to the changes in revenues and expenses described above, overhead costs for administration have been allocated to each of the components listed above.

3.6 Sources and Uses

The table below summarizes the Sources and Uses for the financial proforma.

(in $ millions)	Nominal
Sources	
OSEG Min. Equity	30.0
OSEG Additional Equity	26.3
Construction Loan	97.8
Retail Loan	117.6
Operating Revenues	1649.8
Total	1921.5
Uses	
OSEG Mobilization and Planning Costs	6.0
Retail (including Parking) Construction Costs	126.6
Construction Loan (Principal Repayment)	97.8
Construction Loan (Financing Costs)	5.1
Retail Loan (Principal Repayment)	117.6
Retail Loan (Financing Cost)	121.6
License Fee for Hockey and Football	17.0
Operating Expenses	1115.5
Net Cashflow to Waterfall	314.4
Total	1921.5

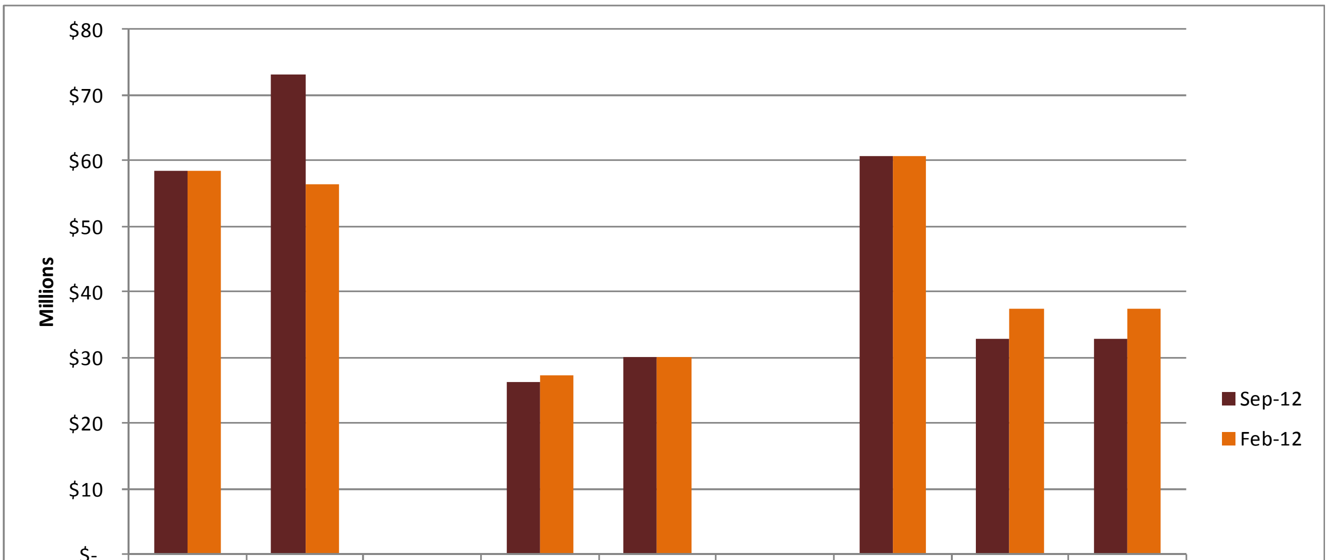
3.7 Impact on Equity and Waterfall Payments

Total waterfall payments are expected to increase from approximately $307.6 million to $314.4 million, an increase of approximately $6.7 million, on a nominal basis over the term of the Stadium Lease. OSEG's payments are expected to increase by $11.2 million, whereas the City's payments are expected to decrease by approximately $4.5 million.

Waterfall summary[5]	**Current**	**Feb 2012**	**Difference**
City Share ($)	$152.1 M	$156.6 M	-$4.5 M
OSEG Share ($)	$162.2 M	$151.0 M	$11.2 M
Total	$314.4 M	$307.6 M	$6.7 M

The chart presented below shows the current waterfall distribution at all levels and the corresponding waterfall distribution in February 2012.

[5] Totals/differences may be off due to rounding.



	Waterfall L1 - Additions to Lifecycle Fund	Waterfall L2 - Distributions to OSEG - return on equity	Waterfall L2 - Distributions to City - return on funding equity	Waterfall L3 - Return of Additional Equity to OSEG	Waterfall L4 - Return of Equity - OSEG	Waterfall L4 - Return of City Funding Equity	Waterfall L5 - Distributions to City - return on deemed equity	Waterfall L6 - Distributions to OSEG - net cash share	Waterfall L6 - Distributions to City - net cash share
Sep-12	$59	$73	$-	$26	$30	$-	$61	$33	$33
Feb-12	$58	$56	$-	$27	$30	$-	$61	$37	$37

- L1: Additions to Lifecycle Fund – as noted previously, the lifecycle cost has increased due to revised assumptions and amended lifecycle contribution term.
- L2: Return on Equity – net cash flow to the waterfall is now realized later in the agreement, which has delayed the return of OSEG's equity, and increased the cumulative return on their equity.
- L3: Return of Additional Equity –reduced by approximately $1 million as a result of changes to the increased amount of construction financing that can be achieved.
- L4: Return of Equity – no change, minimum equity contribution remains at $30 million as per the project agreement.
- L5: Return on Deemed Equity – no change
- L6: Cash share – the increase in total cash flow to the waterfall and the increase in the return at L2 has yielded a total reduction of approximately $4 million to each of the City and OSEG.

4. Revenue Neutrality

The share of the City's realty taxes levied from the commercial tenants at the redeveloped Lansdowne site that are required to offset its debt servicing costs (net of avoided costs and waterfall payments) has been used in previous presentations to convey the incremental cost of the LPP to the City. This analysis is reproduced below:

	Nominal	**Net Present Value**

	Nominal		Net Present Value	
	Current	**Feb-12**	**Current**	**Feb-12**
Avoided costs	$114.0 M	$114.0 M	$48.0 M	$48.0 M
Waterfall payments	$93.6 M	$98.1 M	$22.6 M	$24.1 M
Sub total	$207.6 M	$212.1 M	$70.7 M	$72.2 M
Total debt servicing	-$209.7 M	-$206.2 M	-$88.4 M	-$86.9 M
Sub total	-$2.1 M	$6.0 M	-$17.7 M	-$14.7 M
Property taxes	$181.6 M	$175.8 M	$69.6 M	$67.4 M
Required from taxes	1%	-3%	25%	22%

- Avoided costs: unchanged.
- Waterfall payments: payments to the City from the waterfall have decreased both on nominal and on present value basis.
- Property taxes: total property taxes paid to the City have increased both on nominal and on present value basis.
- Total debt servicing: the City's total debt servicing costs have increased both on nominal and present value basis due to the increase in project costs for the Stadium, Office and Residential components (net of recoveries from the Residential and Office developer). This is partially offset by a decrease in the City's interest rate from 4.63% to 4.25%. The interest rate is reduced due to the following factors.
  - The Infrastructure Ontario lending rate to municipalities for 40 year fully amortizing debt has dropped from 3.93% in February 2012 to 3.85%[6]; and
  - The assumed contingency has been reduced from 0.70% to 0.4%.

Based on the analysis of the changes arising since February 2012, 1% of property taxes from the Retail and Office tenants on the Lansdowne site are expected to be required on a nominal basis to fund the City's debt charges net of avoided costs and waterfall payments. On a net present value basis, 25% of property taxes from the new Retail and Office tenants will be required to fund the City's debt charges net of avoided costs and waterfall payments.

[6] Accessed from http://www.infrastructureontario.ca/Templates/RateForm.aspx?ekfrm=2147483942&sector=mun on 23 September 2012.

Appendix A: the Closed Financial System

	Capital Costs Included in the Closed System	Operating Cash Flows Included in the Closed System /Excluded
Stadium and Arena	Development cost included in closed system as City Funding Equity	Cash flow from operations and annual contributions to the stadium lifecycle reserve are included in the closed system.
Retail and Mixed Use Area	Development cost net of permanent financing included in the closed system as either Minimum or Additional Equity. Land value is recognized in the closed system as the City's deemed equity.	Net cash flow from operations is included in the closed system.
Professional Sports Teams	Acquisition costs (including start-up costs) are included in the closed system as either Minimum Equity or Additional Equity.	Net cash flow from operations is included in the closed system.
Residential Development	Development cost borne by residential developer, not included in closed system. Sale of air rights paid to the City is included in the closed system by way of the City's Funding Equity.	Not included in the closed system.
Office Development	Development cost borne by office developer, not included in the closed system.	Base rent payable through the office head lease is included in the closed system.
Urban Park	Total development cost not part of the closed system.	Total annual operating and maintenance requirements not included in the closed system.