



Preamble

This Consolidated Policy reflects and amends certain policies and priorities respecting the leasing of commercial real property, viz:

1. Nunavut Land Claims Agreement (Article 24)
2. Leasing of Real Property, including Appendix A - Leasing Guideline, dated November 6, 2002
3. Leasing Practices pursuant to the Lease Activity Report
4. Government of Nunavut Space Allocation Standards
5. Government contract regulations, Directive No. 9904
6. Nunavummi Nangminiaqtuniq Ikajuuti Policy, dated April 20, 2006, Section 13.0 Leases – Special Provisions

1. Statement of Policy

The Government of Nunavut provides office space, and other facilities in support of government programs and services. The Government of Nunavut may either lease or own these facilities.

This Policy outlines the process and establishes departmental responsibilities for leasing of real property to meet government requirements for program delivery. Real property includes land and physical structures situated on land.

With respect to leasing, the contractual agreement between the parties may be classified as either operating or capital in nature depending on the substance and underlying intent of the agreement. Each type of lease has different fiscal implications to the GN and therefore warrants further consideration¹.

This Leasing of Real Property Policy is to be reviewed every three years to reflect best leasing practices, current market changes, and relevant Government of Nunavut needs. Likewise, the completion of a needs assessment respecting GN's future long-term program and service facility requirements will also be performed on a three year basis.

2. Principles

The acquisition of real property must be justified (see [Guideline 7](#)) by program needs and the decision on whether to lease or to purchase must be determined by the most economical and beneficial means for fulfilling the identified need. This requires a thorough assessment of the associated costs (see [Guideline 3](#)), risks and benefits.

¹ For more details, please refer to the Leasing Guidelines, Section 9 Fiscal Considerations



A lease agreement should not obligate the Government to pay more than the cost to purchase the real property directly. A premium will be acceptable only if leasing creates tangible benefits sufficient to offset any additional cost.

Whenever leasing is proposed, the following principles will apply:

- a) Leasing should impose no greater cost than outright purchase. Any exceptions must clearly identify tangible benefits arising from the lease that offset the additional cost and any inherent risks borne by the GN.
- b) Leased property shall meet acceptable standards for design, construction, and maintenance as defined by the GN.
- c) Leased property shall be energy efficient as defined by the GN and shall meet any other specific requirements and standards (e.g. environmental) as may be provided.

3. Scope

This Policy applies to all parties involved in the leasing of real property funded by the Government of Nunavut, whether capital or operating in nature.

Exclusions

This Policy does not apply to:

1. Staff Housing Accommodations;
2. Daily or weekly rentals of conference rooms, meeting rooms and court services areas;
3. Municipal properties;
4. Revenue leases; or
5. Unimproved land.

4. Authority and Accountability

Nothing in this Policy shall in any way be construed to limit the prerogative of the Executive Council to make decisions or take action respecting the leasing of improved real property outside the provisions of this Policy. Government is committed to transparency and accountability in leasing activities and as such shall disclose any instances in the Lease Activity Report where Executive Council exercises prerogative.



Responsibilities

a) Program Departments/Leasing Entity

Each department or Leasing Entity is accountable for the provision of programs and services within its mandate and is responsible for identifying its requirements to deliver programs and services consistent with GN Space Allocation Standards. Where this relates to the leasing of real property, CGS or the Leasing Entity will review the requirements and analyze the options and will work with the sponsoring department to prepare a joint submission to FMB, inclusive of all lease-affiliated operating and maintenance costs, as described in, but not limited to, [Guideline 4](#).

b) Community & Government Services (CGS)

CGS/Leasing Agency is the contract authority for commercial real property lease contracts and for related contracts for construction² and goods and services³. CGS provides contracting expertise through its Government Services Branch and also sets government-wide contracting policy and procedures and is responsible for the application of Nunavummi Nangminiqaqtunik Ikajuuti (NNI) Policy, for areas falling within the CGS mandate. The department also provides technical expertise with respect to infrastructure and long term planning of capital requirements. Any department considering the acquisition of real property must engage CGS to work jointly in setting out its formal specifications.

CGS/Leasing Entity is responsible for issuing invitations to tender⁴ for real property leases or pursuing requests for proposals⁵, whichever it deems most appropriate.

Where the total consideration of the lease agreement and any associated agreements exceed \$1,000,000, CGS and the sponsoring department will jointly seek FMB approval to lease.

c) Department of Finance

The Expenditure Management Branch provides policy direction and support to departments and is responsible for providing an independent review of FMB submissions.

² Per FAM Directive No. 9904-25(a), except as specified under 9904-25(b) and unless delegated under 9904-3.

³ Further, where goods or services forms an integral part of a construction contract, it will be deemed a construction contract and be subject to FAM directive No. 9904-25 and NNI.

⁴ Per FAM Directive No. 9904-8(1).

⁵ Per FAM Directive No. 9904-14(1).



d) Department of Justice

The Department of Justice is the legal authority for real property lease contracts and is to have the right of oversight, review and input from a legal perspective therein. Such legal review to comprise, but not be limited to, the following:

- i. CGS reviews all lease-related legal issues with Justice, as they may occur from time to time throughout the term of the lease;
- ii. Justice provides legal advice to CGS respecting all lease-related issues on an ongoing, as required basis;
- iii. Justice works with CGS to draft, review and issue all Letters of Intent (LOIs);
- iv. Justice approves all lease agreements and related documents prior to their execution;
- v. Justice acts as Legal Counsel to CGS where formal representation is required, either in presence or in written form.

e) Financial Management Board (FMB) / Executive Council (EC)

FMB is empowered under the Financial Administration Act (FAA) to “act on all matters related to the financial management and financial administration of the Government⁶” and to issue directives respecting such matters.

FMB must approve all leases where the lease obligations or the value of the property to be leased exceeds \$1,000,000.

FMB may amend the Leasing Guidelines, as may be required from time to time. FMB may also require CGS/Leasing Entity or program departments to report on outstanding leasing matters periodically.

Executive Council may amend the Leasing Policy, as may be required from time to time. FMB may also require CGS/Leasing Entity or program departments to report on outstanding leasing matters periodically.

5. Definitions

In this policy,

- a) **Annual Rental Value** is deemed to include base rent and additional rent;

⁶ Per Sections 4 and 5 of the Financial Administration Act.



- b) **Architectural or engineering services** means architectural or engineering services required in the planning, design, preparation or supervision of the construction of a work or structure;
- c) **Business Incentive Policy** means the Nunavummi Nangminiqaqtuniq Ikajuuti Policy, NNI, of the Government of the Nunavut, as amended from time to time, that provides incentives to northern businesses and includes any directive issued pursuant to that policy;
- d) **Capital Lease** – an agreement which, from the perspective of the lessee (the GN), transfers substantially all the benefits and risks incident to ownership of property to the lessee⁷;
- e) **Construction** means work to build, supply, repair, renovate, restore, maintain or demolish a structure and the hiring of equipment necessary for that work;
- f) **Contract** means a contract for the supply of goods, services, real property or construction, whether by way of sale, conditional sale, lease or otherwise;
- g) **Contract authority** means, unless otherwise stated, (i) a Minister, or (ii) a Deputy Minister, and includes a public officer who has been delegated the powers and duties of a contract authority pursuant to section 4⁸;
- h) **Discount Rate** – the discount rate to be used by the GN, for the purposes of this Policy, is the Government of Canada borrowing rate plus an adjustment factor, if deemed appropriate⁹;
- i) **Estimated Useful Life** – remaining estimated life (in years) over which benefits of use (tenancy) the asset (i.e. building) will provide to the tenants;
- j) **Fair Market Value** - The total price (cash or equivalent) that Government could reasonably be expected to pay and a lessor (seller) could reasonably be expected to accept, if the property were for sale on the open market for a reasonable period of time, both Government and lessor (seller) being in possession of all pertinent facts, and neither being under any compulsion to act;
- k) **Financial Management Board** means the Financial Management Board as established by the Legislative Assembly and Executive Council Act;
- l) **Goods** means materials, goods or equipment, whether in existence or not at the time of the contract;

7 From Definitions provided in CICA Handbook Section 3065 “Leases”.

8 Section 4 Leasing of Real Property – Consolidated Policy: Authority and Accountability

9 The adjustment factor will be reviewed periodically by the Department of Finance and any revisions will be communicated.



- m) **Inuit firm** means an entity which complies with legal requirements to carry on business in the Nunavut settlement area, and which is:
- i. a limited company with at least 51% of the company's voting shares beneficially owned by Inuit, or
 - ii. a Co-operative controlled by Inuit, or
 - iii. an Inuk sole proprietorship or partnership; and
 - iv. able to present evidence of inclusion on NIT's Inuit Firms Registry;
- n) **Invitation to tender** means a written invitation to tender in which the format and the nature of the tender are stipulated; which will include an offer to lease, accomplished by public advertisement or private invitation;
- o) **Lease Cost Premium** is the amount by which the present value cost of leasing exceeds the purchase price of the real property;
- p) **Leased Tangible Capital Asset** – a non-financial asset that has physical substance and a useful life extending beyond an accounting period and is held under lease by a government for use, on a continuing basis, in the production or supply of goods and services¹⁰;
- q) **Lease-To-Own Contract** - a lease where the owner agrees to sell the property to the Government of Nunavut upon termination of the lease contract (see [Guideline 2](#));
- r) **'Lease versus Own' Analysis** – A discounted cash flow analysis that compares the present value cost of leasing versus the capital cost of purchasing the real property;
- s) **Lessee** – a person who holds the lease of a property;
- t) **Lessor** – a person who leases or lets a property to another;
- u) **Operating Lease** – an agreement in which the legal owner (lessor) of the property does not transfer substantially all the benefits and risks incident to ownership of property¹¹;
- v) **Person** includes a corporation, government organization, NGO, partnership, or proprietorship;

¹⁰ From CICA Public Sector Guideline 2 "Leased Tangible Capital Assets (April 2000)

¹¹ From Definitions provided in CICA Handbook Section 3065 "Leases".



- w) **Present Value Cost** – the amount that represents the value of future payments in today’s dollars, applying the appropriate discount rate;
- x) **Proposal** means an offer to provide goods, services or construction that is submitted to a contract authority in response to a request for a proposal;
- y) **Real Property** – Land and physical structures (e.g. facilities or improvements situated on land);
- z) **Request for proposal** means the solicitation of a proposal, to include an offer to lease, accomplished by public advertisement or private invitation;
- aa) **Revenue Lease** - a lease to non-Government of Nunavut tenants, to Government of Nunavut employees and to certain Government of Nunavut departments, boards and agencies for which there are rental payments made by the tenant to the Government of Nunavut;
- bb) **Significant Lease Agreement** – a lease with a term of 10-years or more, and/or respecting property with a value of \$1,000,000 or greater;
- cc) **Term** – the contractual “term” (as specified in the lease agreement) ... and includes the term of any renewal of that lease¹².

In addition, where any of the following provisions apply, the term should, at a minimum, reflect:

- i. all periods covered by bargain renewal options (e.g. renewals at less than fair market value)
- ii. all periods for which failure to renew would impose on the lessee (the GN) a penalty sufficiently large that renewal appears reasonably assured
- iii. all periods covered by ordinary renewal options during which the lessee (the GN) has undertaken to guarantee the lessor’s debt related to the leased property
- iv. all periods covered by ordinary renewal options preceding the date on which a bargain purchase option (e.g. purchase at less than fair market value) is exercisable
- v. all periods representing renewals or extensions of the lease at the lessor's option provided the lease term does not extend beyond the date a bargain purchase option becomes exercisable¹³.

¹² From the Treasury Board Secretariat publication “Real Property Glossary” (July 1, 2001)



6. Policy Provisions

Financial Resources

- 6.1 Financial resources required under this Policy are conditional on approval of funds in the Main Estimates by the Legislative Assembly and there being a sufficient unencumbered balance in the appropriate activity for the fiscal year for which the funds would be required.

Lease Criteria

- 6.2 Properties will be leased according to the following criteria:
- (a) The private sector is ready, willing, and able to provide properties for leasing.
 - (b) The property is of a type appropriate for leasing by the government.
 - (c) Financial Management Board approved **all** lease agreements where the lease obligations (sum total of lease payments over the term of the lease) or the value of the property to be leased exceeds \$1,000,000.
 - (d) Leased properties are to be operated and maintained in accordance with the same operations and maintenance standards applied to government-owned properties.
 - (e) The present value cost of leasing not to exceed the purchase price of the real property, except as deemed appropriate and required in the support of development of northern business, or where there are sufficient tangible benefits to offset the lease premium. Only Executive Council and/or the Financial Management Board may authorize the award of a lease contract where the lease cost premium exceeds ten percent of the cost of ownership.
 - (f) Where the lease cost premium exceeds ten percent, the Minister (or designate) may consider negotiating a lease-to-own contract in order to reduce the premium. In such instances, the Minister will return to FMB with the options for consideration.

New Lease Contracts

- 6.3 Prior to committing to a significant lease agreement, GN must refer to the most recently conducted needs assessment, or in its absence, perform a needs assessment respecting its future long-term government program and service facility requirements. Such a needs assessment should be undertaken on a timeline consistent with the negotiation timeline pursuant to Appendix A.



- 6.4 All newly-leased properties will be acquired through invitation to tender or public proposal calls, except where the Executive Council has otherwise authorized negotiations to commence. Invitations to tender and requests for proposals will provide opportunities to Inuit firms, in accordance with Article 24 of Nunavut Land Claims Agreement and NNI Policy. Designated Inuit Organizations (Qikiqtani Inuit Association, Kivalliq Inuit Association, and Kitikmeot Inuit Association) will be provided with copies of the Invitation to Tender or Request for Proposal.
- 6.5 During negotiations, no GN employee is permitted to make representations, verbal or written, to a lessor, other than through a formal Letter of Intent or Offer to Lease.
- 6.6 The Executive Council may authorize the awarding of new lease contracts to businesses with other than the lowest bid.
- 6.7 Where an invitation to tender or request for proposals has been issued, the Minister (or designate) may negotiate with the lowest bidder to reduce lease costs and may negotiate a lease-to-own contract.
- 6.8 Where the Executive Council has directed lease negotiations, the Minister (or designate) may negotiate a lease-to-own agreement in order to reduce the lease cost premium.
- 6.9 Adherence to this leasing policy is to be ensured by completing the Appendix B checklist. The checklist shall be appended to and form part of every file.
- 6.10 To ensure compliance with this leasing policy, all checklists and related working paper files are to be reviewed and approved by the authorized signing authority prior to executing a lease agreement.
- 6.11 FMB Recommendations and Record of Decision documents must be dated, signed, signatory identified by name (typed/printed), with all pages numbered.

Lease Renewals

- 6.12 The requirement for, and the needs and term of, a lease renewal must be confirmed by the Minister (or designate) responsible prior to commencement of renewal-related negotiations.
- 6.13 Prior to committing to significant lease (renewal) agreements, GN must refer to the most recently conducted needs assessment, or in its absence, perform a needs assessment respecting its future long-term government program and service facility requirements. Such a needs assessment should be undertaken on a timeline consistent with the negotiation timeline as recommended in Appendix A.



- 6.14 The GN must commence lease renewal negotiations commensurate with the significance (annual value and term) of the commitment. Timing of negotiations to be pursuant to Appendix A.
- 6.15 During negotiations, no GN employee is permitted to make representations, verbal or written, to a lessor, other than through a formal Letter of Intent or Offer to Lease.
- 6.16 Adherence to this leasing policy is to be ensured by completing the Appendix B checklist.
- 6.17 To ensure compliance with this leasing policy, all checklists and related working paper files to be reviewed and approved by the authorized signing authority prior to a executing a lease agreement.
- 6.18 FMB Recommendations and Record of Decision documents must be dated, signed, signatory identified by name (typed/printed), with all pages numbered.

‘Lease versus Own’ Analysis

- 6.19 The Minister (or designate) will undertake a ‘lease versus own’ analysis of all proposed new lease contracts with terms of ten years or more, and/or respecting real property with a value of \$1,000,000 or greater.
- 6.20 It is the responsibility of CGS/Leasing Entity to ensure that its request to FMB contains complete and sufficient detail to enable a full and comprehensive analysis by Finance staff. All relevant supplementary information on financial details or to explain issues referenced in the submission must be appended, to the full satisfaction of Expenditure Management Branch.
- 6.21 A ‘lease versus own’ analysis must be prepared by CGS/Leasing Entity for submission to FMB, to comprise the following components:
- Identification of the lease premium, if any and a full discussion of offsetting (quantifiable) benefits
 - Risk assessment, noting which party bears responsibility for each type of risks identified
 - Full disclosure of acquisition costs
 - Full disclosure of lease agreement terms and conditions
 - Sign-off from Finance, including any recommendations or concerns based on its objective review.



Lease Agreements

- 6.22 Prior to executing a Letter of Intent and a lease agreement, and subsequent to negotiation, the lease agreement is to be subject to review by legal counsel and approval by FMB.

Real Property Lease Operating & Maintenance Costs

- 6.23 Operating and maintenance costs reimbursement to landlord to be subject to due diligence and verification procedures pursuant to [Guideline 4](#), prior to approval and payment.

Sunset Clause

- 6.24 This policy shall be in effect from the date of the signature until December 30, 2010.

Premier

LEASE NEGOTIATION TIMING

Annual Rental Value ¹⁴	or	Term of Lease	Commencement of Negotiations	Conclusion of Negotiations
< \$250k		< 36 months	6 months prior to expiry date of lease	3 months prior to expiry date of lease
> \$250k < \$500k		3 years < 5 years	12 months prior to expiry date of lease	3 months prior to expiry date of lease
> \$500k < \$1M		5 years < 10 years	24 months prior to expiry date of lease	12 months prior to expiry date of lease
> \$1M < \$1.5M		10 years < 15 years	36 months prior to expiry date of lease	24 months prior to expiry date of lease
> \$1.5M		> 15 years	60 months prior to expiry date of lease	36 months prior to expiry date of lease

¹⁴ See Section 5: Definitions

PROPERTY LEASE POLICY COMPLIANCE CHECKLIST

NEW LEASE AGREEMENTS

*** It is expected that policy adherence is to occur, which will be evidenced by answering “yes” or “n/a” to the following questions. If “no” is answered, then FMB approval is required prior to proceeding further with the lease agreement.**

<u>Procedure</u>	<u>Done</u>		
	<u>Yes</u>	<u>No *</u>	<u>n/a</u>
1. Is the contemplated (new) lease a significant lease agreement (<i>greater than 10-year term, and/or respecting property with a value of \$1,000,000 or greater</i>)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
° If no, proceed to point 3 of this checklist			
° If yes, proceed to point 2 of this checklist			
2. Has the needs assessment been completed?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
3. Has an Invitation to Tender or Request for Proposals been issued respecting this new lease requirement?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
4. Is the Invitation to Tender or Request for Proposals in accordance with the Nunavut Land Claim Agreement Article 24 and the NNI Policy?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
5. Have RFP responses, which must include an offer to lease, been received and reviewed in detail?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
6. Do the prospective new lease related real properties meet substantially all of the needs as identified in the RFP and/or in the needs assessment (if applicable)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
7. Has an assessment of the RFP responses been made?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Such an assessment should consider the following:			
° Meeting substantially all of the needs as identified in the needs assessment	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
° Cost of leasing the real property	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
° Implications of other significant terms of the proposed lease agreement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

<u>Procedure</u>	Done		
	<u>Yes</u>	<u>No</u> *	<u>n/a</u>
8. Have negotiations occurred to ensure the minimal lease cost obligation has been obtained?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
9. Has the lease cost premium been calculated, with consideration to Guideline 1 (<i>Net Present Value</i>) and Guideline 3 (<i>cost estimate document</i>)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
10. Have negotiations occurred to reduce the lease cost premium?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
11. If this is a significant lease, or as otherwise directed by the Minister (or designate), then has a 'lease versus own' analysis been undertaken, pursuant to Guideline 2 .	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
12. Has the negotiated Letter of Intent and/or Lease Agreement been subject to legal counsel review and approval?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Supporting working paper file to comprise the following:

- | | | | |
|--|--------------------------|--------------------------|--------------------------|
| ◦ Needs assessment (refer to Guideline 8) | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ◦ Invitation to Tender or Request for Proposals | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ✓ Invitation to Tender or RFP annotated to indicate compliance with Nunavut Land Claim Agreement Article 24 and the NNI Policy | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ◦ RFP responses | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ✓ Each RFP response annotated to indicate that established criteria have been met (<i>pursuant to item 7 above</i>) | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ◦ Landlord-initiated written offer to lease (<i>refer to Guideline 6 for minimum requirements</i>) | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ✓ Documentary evidence of negotiations to ensure minimal lease cost obligation | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |
| ◦ Lease cost premium calculation | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

Appendix B

<u>Procedure</u>	Done		
	<u>Yes</u>	<u>No</u> *	<u>n/a</u>
<ul style="list-style-type: none"> ✓ Documentary evidence of negotiations respecting lease cost premium reduction 	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<ul style="list-style-type: none"> ◦ 'Lease versus own' analysis 	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<ul style="list-style-type: none"> ◦ Legal opinion respecting negotiated lease agreement 	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
<p>All working papers dated and initialled by preparer</p>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Completed by: _____ Date: _____
(print name) *(signature)*

Approved by: _____ Date: _____
(print name) *(signature)*

PROPERTY LEASE POLICY COMPLIANCE CHECKLIST

LEASE RENEWALS

*** It is expected that policy adherence is to occur, which will be evidenced by answering “yes” or “n/a” to the following questions. If “no” is answered, then FMB approval is required prior to proceeding further with the lease agreement.**

<u>Procedure</u>	<u>Done</u>		
	<u>Yes</u>	<u>No *</u>	<u>n/a</u>
1. Is the timing of lease renewal negotiations being followed, pursuant to Appendix A?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
2. Has the Minister (or designate) provided written authorization to commence renewal of lease negotiations?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
3. Is the lease renewal a significant lease agreement (<i>greater than 10-year term, and/or respecting property with a value of \$1,000,000 or greater</i>)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
° If no, proceed to point 5 of this checklist			
° If yes, proceed to point 4 of this checklist			
4. Has the needs assessment been completed?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
5. Has an Invitation to Tender or Request for Proposals been considered respecting this renewal of lease requirement?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
6. Is the Invitation to Tender or Request for Proposals in accordance with the Nunavut Land Claim Agreement Article 24 and the NNI Policy?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
7. Have RFP responses, which must include an offer to lease, been received and reviewed in detail?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
8. Has an assessment of the RFP responses been made?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Such an assessment should consider the following:			
° Meeting substantially all of the needs as identified in the needs assessment	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
° Cost of leasing the real property	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

<u>Procedure</u>	Done		
	<u>Yes</u>	<u>No</u> *	<u>n/a</u>
◦ Implications of other significant terms of the proposed lease agreement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
9. Do the prospective new lease related real properties meet substantially all of the needs as identified in the RFP and/or in the needs assessment (if applicable)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
10. Have negotiations occurred to ensure the minimal lease cost obligation has been obtained?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
11. Has the lease cost premium been calculated, with consideration to Guideline 1 (<i>Net Present Value</i>) and Guideline 3 (<i>cost estimate document</i>)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
12. Have negotiations occurred to reduce the lease cost premium?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
13. If this is a significant lease, or as otherwise directed by the Minister (or designate), then has a 'lease versus own' analysis been undertaken, pursuant to Guideline 2 .	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
14. Has the negotiated lease agreement been subject to legal counsel review and approval?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
Supporting working paper file to comprise the following:			
◦ Documentation of lease renewal negotiation timeline	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ Ministerial authorization to commence lease renewal negotiations	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ Needs assessment (refer to Guideline 8)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ Invitation to Tender or Request for Proposals	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
✓ Invitation to Tender or RFP annotated to indicate compliance with Nunavut Land Claim Agreement Article 24 and the NNI Policy	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Appendix C

<u>Procedure</u>	Done		
	<u>Yes</u>	<u>No</u> *	<u>n/a</u>
◦ RFP responses	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
✓ Each RFP response annotated to indicate that established criteria have been met (<i>pursuant to item 8 above</i>)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ Landlord-initiated written offer to lease (<i>refer to Guideline 6 for minimum requirements</i>)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
✓ Documentary evidence of negotiations to ensure minimal lease cost obligation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ Lease cost premium calculation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
✓ Documentary evidence of negotiations respecting lease cost premium reduction	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ ‘Lease versus own’ analysis	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
◦ Legal opinion respecting negotiated lease agreement	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
All working papers dated and initialled by preparer	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

Completed by: _____ Date: _____
(print name) *(signature)*

Approved by: _____ Date: _____
(print name) *(signature)*

Present Value Calculation Guideline

Purpose of Present Value Calculation:

The present value calculation quantifies the total investment in the building to which the lease relates, that is required over the term of the lease, stated in today's dollars.

Knowing this amount will allow GN (the lessee) to assess its 'lease versus own' the building options, such as:

1. Proceed or not proceed with the lease
2. Renegotiate the terms of the lease
3. To assess the present value against the fair market value of the building – is this lease arrangement “a good deal”
4. To consider an outright purchase of the building or a lease-to-own
5. To consider new building (replacement) construction

Present Value Calculation:

The present value calculation should include the following components:

Component	Explanation/Definition
1. Term	Usually represented in number of years or months, dependant on the payment period (i.e. annual lease payments or monthly lease payments).
2. Base Lease Payments	The amount paid on a periodic (i.e. annual payment, monthly payment) basis, usually the amount identified as the minimum lease payment pursuant to the lease agreement, exclusive of common area costs and the recoverable GST. <i>Note: The timing of the payment respecting the period need to be identified as either at the beginning or at the end of the period. For most leases, the beginning of period is applicable.</i>
3. Discount Rate (factor)	This discount rate is expressed as an annual interest rate, usually representing the average cost of borrowing (debt) that the GN would incur were it to borrow to make such a capital purchase. GN has historically used for discount purposes the existing 10-year Government of Canada bond rate.

Sample Calculation of Present Value

Capital cost \$ 17,815,892
 Base lease payment (per yr) \$ 729,520 Years 1 - 10
 \$ 779,260 Years 11 - 20
 Interest rate
 Government borrowing rate: 5.25%

Term (Yrs)	Base Lease Payments	Discount Rate (Factor)	Present Value
1	729,520.00	0.9501188	693,130.64
2	729,520.00	0.9027257	658,556.43
3	729,520.00	0.8576966	625,706.82
4	729,520.00	0.8149136	594,495.79
5	729,520.00	0.7742647	564,841.61
6	729,520.00	0.7356435	536,666.61
7	729,520.00	0.6989486	509,897.02
8	729,520.00	0.6640842	484,462.72
9	729,520.00	0.6309589	460,297.12
10	729,520.00	0.5994859	437,336.94
11	779,260.00	0.5695828	443,853.08
12	779,260.00	0.5411713	421,713.14
13	779,260.00	0.5141770	400,677.56
14	779,260.00	0.4885292	380,691.27
15	779,260.00	0.4641608	361,701.92
16	779,260.00	0.4410079	343,659.78
17	779,260.00	0.4190098	326,517.61
18	779,260.00	0.3981091	310,230.51
19	779,260.00	0.3782509	294,755.83
20	779,260.00	0.3593833	280,053.04

Present Value of lease payments	9,129,245.44	
Capital cost	17,815,892.00	
Cost difference if leased	<u>(8,686,646.56)</u>	
Lease Cost Premium (%)	<u>(8,686,646.56)</u>	-48.8%
	17,815,892.00	

‘Lease versus Own’ Analysis

Ownership through a Lease Agreement should be premised on:

<u>Principle</u>	<u>Calculation</u>
1. GN must recover its investment in the property, plus a return on the investment.	$\frac{\text{Present value of the lease payments over the term of the lease}}{\text{Fair market value of the real property subject to lease}} \geq 90\%$
2. GN must obtain the majority of (ownership) benefits associated with the building during the term of the lease.	$\frac{\text{Lease term (total number of years)}}{\text{Estimated remaining useful life (in years)}} \geq 75\%$

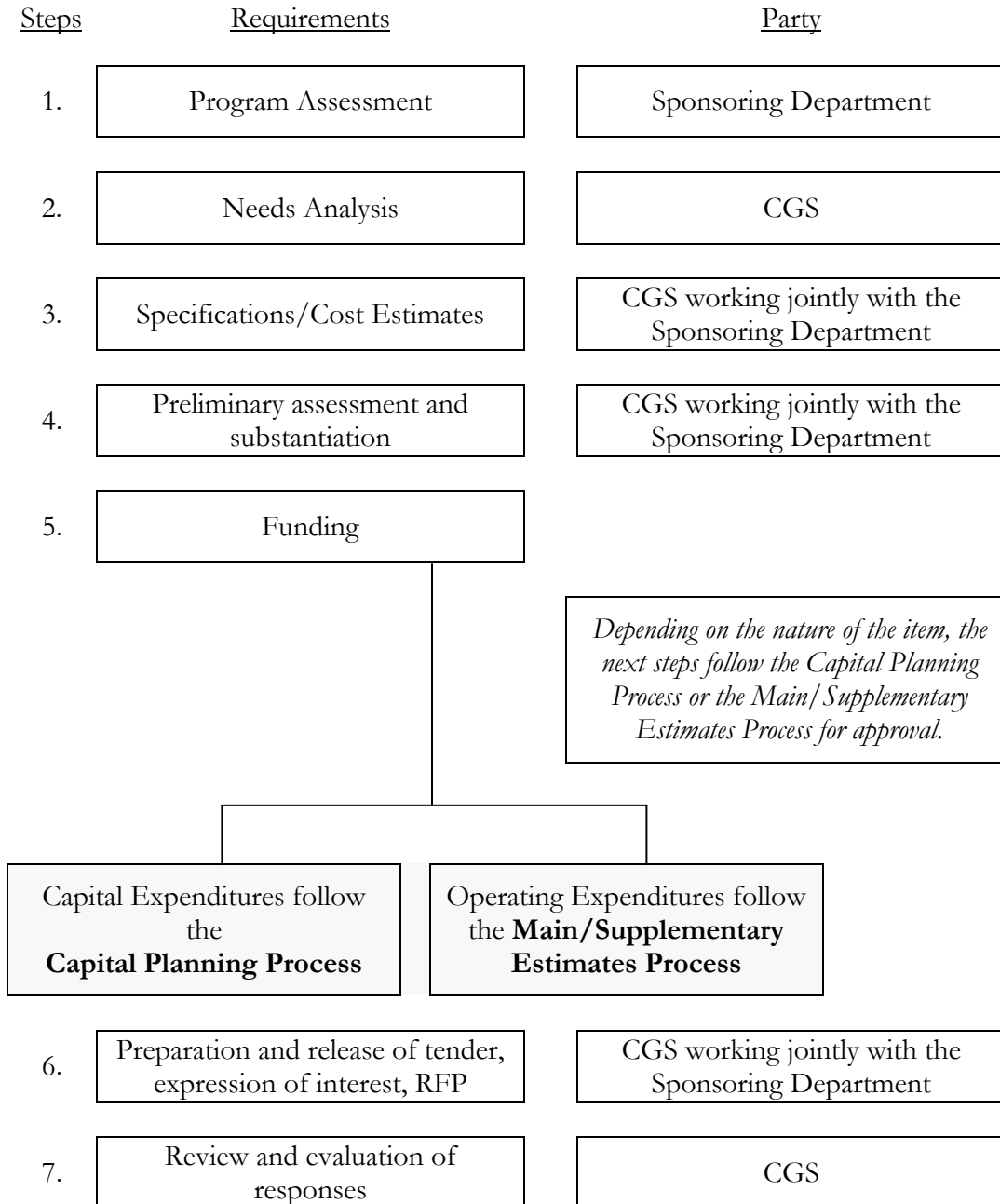
The above noted threshold amounts are approximate minimum requirements.

‘Lease versus Own’ Analysis – Required Documentation:

- Net present value analysis, pursuant to present value calculation– see [Guideline 1](#)
- Fair market value (appraisal) of the real property subject to lease (for purposes of assessing a purchase price from the landlord); normally derived from an appraisal as conducted by a qualified appraiser, within the last twelve months
- Comparable building construction quotes – supported by the appropriate cost estimate classification (see cost estimate document [Guideline 3](#))
- Estimated remaining useful life of the real property subject to lease; estimated remaining useful life is usually the period over which the asset (building) is amortized (expenses) on the Statement of Rental Operations.
- Consideration of other building lease or purchase options, based on the RFP responses and GN’s assessment

The following flowchart outlines the steps involved in the proposal development and identifies who should be engaged and at which stage. This corresponds with the roles and responsibilities set out in the GN *Leasing of Real Property - Consolidated Policy*.

Acquisition



Financing

8.	Preparation of 'lease versus own' analysis, benefit/risk assessment, review of fiscal considerations, etc.	CGS and Sponsoring Department working jointly to prepare FMB submission (where required) and supporting analysis
9.	Review of FMB submission and supporting analysis	Finance to provide comments
10.	Approval of financing decision	FMB

Finalization

11.	Contract preparation and execution	CGS
-----	------------------------------------	-----

Notes re:

Step #8 Such analysis is required to support **all** 'lease versus own' decisions, irrespective of contract value. However, the level of analysis may vary relative to project complexity and the risk to the GN.

Step #9 An FMB submission is required where the financing decision exceeds the \$1,000,000 threshold. Finance is required to review same and provide comments, as appropriate. In addition, Finance may be consulted and/or provide input on the analysis to support a 'lease versus own' decision which falls below the \$1,000,000 threshold.

Step #10 An FMB decision is required for 'lease versus own' decisions which exceed the \$1,000,000 threshold. This is a separate decision from any FMB approval of interdepartmental budget transfers or related matters.

Cost Estimate Document Guideline

For selection of the appropriate class cost estimate, see below for estimate classes. For 'lease versus own' analysis decision purposes, the class D estimate basis is considered the minimum appropriate basis. While some aspects of detail by classification of cost estimates may vary, to some extent by industry expert, this summary of classification is deemed acceptable for purposes of this policy.

CLASSIFICATION OF COST ESTIMATES. There are six classifications of cost estimates: Class A, B, C, D, F and X.

Class A - Detailed Cost Estimate. An extensive cost estimate based on detailed engineering drawings, material lists and man-hours by required skills and trades. The level of detail addressed in a Class A estimate should be to the maximum extent feasible. **Variance is not expected to exceed 10 percent.**

Class B - Estimate. This estimate is prepared after site investigations and studies have been completed and the major systems defined. It is based on a project brief and preliminary design. It is used for obtaining approvals, budgetary control and design cost control. **Variance is expected to be 10% – 15% percent.**

Class C - Budget Quality Estimate. This estimate, which is prepared with limited site information, is based on probable conditions affecting the project. It represents the summation of all identifiable project elemental costs. It is used for program planning, to establish a more specific definition of client needs and to obtain preliminary approval. Class C estimates are the recommended level of estimates of cost developed by a field activity to be used in budget submissions. **Variance is not expected to exceed 15 percent.**

Class D - Feasibility Estimate. Class D estimates are required prior to completion of the design or preparation of detailed specifications, reflecting the uncertainty associated with having incomplete information available for estimating purposes. It is usually exploratory in nature and is prepared to perform trade-offs and cost effectiveness analysis. **Variance is not expected to exceed 20 percent.**

Class F - "Ballpark" Estimate. Class F estimates are known as "ballpark" estimates. This is a quick cost estimate prepared in the absence of minimum design and cost information and is based on gross approximations. It is calculated by escalating previous costs to current dollars, using empirical costs for similar work and adding factors for expected changes in design, processes procedures and other economic considerations. Acceptable when higher-level estimates are not possible due to insufficient time or incomplete information. **Variance is not expected to exceed 40 percent.**

Class X - Directed or Modified Estimate. An estimate provided by other Government activities or as directed by higher levels of authority. It is generally a total cost restriction without a developed design, engineering or a detailed cost estimate. A directed estimate is also a modification of any previous cost estimate, Classes A through F, to conform to budget reductions or restrictions on cost which is not based on a change in the scope of work required.

**Diligence and Verification Procedures respecting
Operating & Maintenance Costs**

Verification procedures should include the following:

1. To review the existing lease agreement to ensure that the operating and maintenance costs are recoverable from GN as a tenant – are they within scope of O & M costs?
2. Is there an audit or review requirement of the landlord respecting O & M verification.
3. Is there a base year against which the recovered costs are to be compared (deducted from) for reimbursement purposes?
4. Has an allocation of the operating and maintenance costs been considered, where GN is occupying less than 100% of the building?
5. Are the costs reasonable in comparison to prior years' operating and maintenance recoveries by the landlord?
6. Obtain source documents to support the recovery costs sought by the landlord, and agree amounts billed to GN against these documents.

The following costs represent possible operating and maintenance expenses pursuant to a Real Property Lease Agreement that may be recoverable from GN (the lessee).

Direct Costs

1. Dedicated on-site person years (i.e. a stationary engineer),
2. Heating fuel,
3. Municipal services including garbage pickup, water delivery and sewage collection
4. Supplies and material costs,
5. Contract skilled and unskilled labour costs,
6. Property Taxes
7. Janitorial and cleaning,
8. Snow removal,

Indirect Costs

1. Accumulated incremental person years for facility maintenance management (due to two, three or more facility enhancements – not specifically dedicated to a facility inspections, systems, etc),
2. Electricity,
3. Monthly telecom expenses from service providers,

Guideline 4

4. Contract skilled and unskilled labour costs,
5. Grant in lieu of property taxes,
6. Daily and monthly boiler and electrical inspections, etc.
7. Other miscellaneous items associated with ongoing repairs and maintenance of various systems – electronic, mechanical, etc.

Standard Lease Agreement Letter of Intent – Terms

A Letter of Intent to lease should be prepared in good legal form as prescribed by legal counsel, and should include the following:

1. Real Property description
 - address
 - square footage
2. Term
 - Commencement date
 - Expiry date
 - Renewal options
3. Rent commitment
 - annual and monthly base rent
4. Additional rent
5. Landlord obligations
 - leaseholds, with timing
 - inducements
6. Lessee's obligations
7. Ownership options
 - Bargain purchase
 - First right of refusal
 - Buyout at fair market value
8. Sign off/dating/witnesses
 - By landlord
 - By Lessee
 - Time requirement for confirmation sign off
9. Security deposit

All proposed Letters of Intent should be subject to final review by legal counsel before being formally issued.

Standard Letter of Offer to Lease from Landlord – Terms

A Standard Letter of Offer to Lease should consider the following:

1. Leased Premises
 - a. As office space
 - b. As storage space
 - c. Ingress/egress/common areas
2. Term
3. Option to Extend
4. Pre-term and Delayed Occupancy
 - a. Improvements
5. Rent
6. Parking
7. Taxes
8. Tax Adjustment
9. Assignment
10. Holding Over
11. Services and Equipment
 - a. Hot and cold water to all washbasins and sinks
 - b. Drinking fountain on every floor
 - c. Heat, ventilation, air conditioning, air circulation and humidity control
 - d. Lighting and all electrical power except as specifically otherwise provided
 - e. Fire alarm system
 - f. Auxiliary supply of electricity and power for emergency services and systems
 - g. Dispensary items and deodorant blocks/maintenance and repairs to keep lavatory and toilet equipment and accessories in good operating condition
 - h. Snow and ice removal
 - i. Maintenance and repairs to keep common areas clean and operational
 - j. Garbage/recyclable material removal

- k. Cleaning materials and labour
 - l. Elevator service
 - m. Window and floor covering replacement due to wear and tear
 - n. Access for disabled
12. Signage and Flag Display
13. Operating Costs Adjustment
- a. Operating costs with respect to the basic unit operating rate
14. Default
15. Destruction of Building or Leased Premises
16. Indemnity
17. Insurance
18. Standards of Repair
19. Lessee' Improvements
20. Set-Off
21. Environmental Representations and Warranties
22. Mortgage
23. Notices
24. General

Real Property Acquisition – Justification Process

Justification procedures should consider the following:

1. Purpose
2. Background
3. Need
4. Financial Implications

Needs Assessment – Real Property

The following questionnaire has been developed to assist in assessing:

- ✓ Your current real property needs
- ✓ Your future real property needs

The answers to the following questionnaire will assist in preparing an RFP or Invitation to Tender for new lease and renewal of lease situations.

GN Department Profile

General Information

1. Identify the nature of your departmental or Crown corporation activity (“business”).

2. What is the location of operation?

3. Is the level of business cyclical?

4. How many employees do you have?
 - a. How many working on site?

 - b. How many working remotely?

5. What is the current square footage cost of your current lease?

6. What level of common areas costs is currently incurred?

7. When does the current lease expire?

8. What duration of lease is necessitated by your requirements?

9. Is the management and maintenance of the building addressed by the landlord or by GN staff?

Real Property (Land & Building) Needs

Current Needs

***Future Need
5 - 10 years***

- | | |
|--|--|
| <ol style="list-style-type: none"> 1. How many facilities are required?
_____ | |
|--|--|

Real Property (Land & Building) Needs

Current Needs

**Future Need
5 - 10 years**

2. Square footage and description of each facility		
3. Do the current facilities meet your needs in terms of		
a. occupancy?		
b. storage?		
c. environmental conditions (HVAC)?		
d. parking?		
4. Is space utilization and functionality adequate?		
5. Is storage an important consideration? Is so, what are your requirements?		
6. Are valuable goods stored onsite?		
7. Security & Fire Protection		
a. Is there a need for physical security in the building during or after normal working hours? Does such exist?		
b. Does the building have a fire protection system?		
c. Does 24-hour monitoring exist for:		
i. physical security?		
ii. fire?		
8. Is there a need for wheelchair access?		
9. Do your department's operations (e.g. warehousing, mechanical repairs, hazardous waste storage) present any unique building requirements?		

Completed by: _____ Date: _____
(print name) (signature)

Lease Classification

A lease agreement may be classified as either operating¹⁵ or capital¹⁶ in nature depending on the substance and underlying intent of the agreement. Each type of lease has different implications to the GN and therefore warrants further consideration.

Readers are strongly encouraged to pay due regard to all relevant factors in conjunction with the specific criteria (below) in determining the underlying intent of the agreement and hence the substance and nature of the obligation. In particular, where much additional risk is likely to be borne by the GN (whether or not stipulated in the agreement), this may indicate that, for all intents and purposes, the GN has assumed overall responsibility for the asset through executing the agreement. Where substantial risks and benefits of ownership are assumed, the underlying intent of the agreement would be considered capital in nature.

Specific Guidance

The following is based on the Public Sector Guideline 2 “*Leased Tangible Capital Assets*” issued by the Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants. (Where italicized, the text is a direct excerpt from the guideline.)

The overriding consideration in assessing whether the lease agreement is capital or operating is to identify whether “***substantially all the benefits and risks have been transferred***”, whether or not title has formally passed. If the risks and benefits reside, for the most part, with the lessor, the agreement represents an operating lease to the GN. If the risks and benefits reside with the GN, regardless of legal ownership, the agreement represents a capital lease to the GN.

Paragraph 5:

From the point of view of the government, the benefits and risks of ownership would be transferred to the government when, at the inception of the lease, one or more of the following conditions are present:

- (a) *There is reasonable assurance that the government will obtain ownership of the leased property by the end of the lease term.*

[This would occur where the legal ownership, under the agreement, transfers to the GN at or by the end of the lease term. Alternatively, the GN may have an option to purchase the asset for significantly less than its fair market value (otherwise known as a “*bargain purchase option*”). The terms of the bargain purchase option are considered so favourable that it can be reasonably assured that the option will be exercised. Under either scenario therefore it is assumed that ownership will transfer to the GN.]

- (b) *The lease term is of such duration that the government will receive substantially all of the economic benefits expected to be derived from the use of the leased property over its life span.*

[While the economic (or useful) life of the asset may extend beyond the lease term, it would be assumed that the GN obtains the majority of the economic benefits associated with the asset if the lease term covers usually 75% or more of the asset’s useful life.]

¹⁵ For the definition of an “operating lease”, please refer to Section #7 of the Leasing Guideline.

¹⁶ For the definition of a “capital lease”, please refer to Section #7 of the Leasing Guideline.

- (c) *The lessor would be assured of recovering the investment in the leased property and of earning a return on the investment as a result of the lease agreement.*

[This is assumed to be true if the present value of the minimum lease payments at the beginning of the lease is equal to substantially all (defined typically as 90% or more) of the fair value of the leased property.]

The lease criteria noted above are set out also in a decision tree for convenience. (Please refer to Page 36.)

These criteria have been set out to assess whether the GN, on balance, has assumed the risks and benefits of owning the real property. If so, the lease would be deemed capital in nature.

Additional Considerations

When assessing the appropriate classification of a lease agreement, it is necessary to give due consideration to the nature of the agreement rather than simply its form¹⁷. While the criteria set out in Paragraph 5 above (and summarized in the decision tree which follows) provides the most objective evidence of the underlying intent or substance of the agreement, the analysis of these criteria should be supplemented by a full assessment of other considerations.

It should also be noted that the reliability of the numerical tests contained in Paragraph 5 (b) and 5 (c) above become more questionable the further out the lease term or time horizon extends due to measurement uncertainty. Further it is possible that even if conditions in Paragraph 5 are not present that it would be appropriate to classify the lease as a leased tangible capital asset¹⁸ under conditions set out in Paragraphs 6 and 8-10¹⁹ of the Public Sector Guideline. Therefore it is important to consider all aspects prior to concluding on the appropriate lease classification.

Any related agreements (such as the provision of services for the leased facilities) should also be considered as part in this examination. Where the Government may be paying a premium (e.g. above fair market value) for these services, it may indicate that part of the lease cost has been absorbed in the ancillary contractual arrangement and needs to be adjusted when analyzing the total lease costs, particularly under the Paragraph 5 (c) test and in the determination of the lease premium. Further, any provision for additional rents which can be reasonably estimated at the inception of the lease and are likely to be paid should be included in the lease analysis.

Where the leased real property meets the Government's requirement to provide an essential service or fulfils a very specialized purpose, the benefits and risks of ownership may, for all intents and purposes, have transferred to the GN. This is particularly true where it would not be feasible for any other entity to take over the use of the leased real property and/or where it would not be effective to convert the leased asset to another use, or, if possible, not without incurring significant cost. The provision of a facility in a remote location to meet

17 In the Public Sector Accounting Guideline, this is referred to as "substance over form" and means that the nature or underlying intent of the agreement is more important when determining its classification than how it has been labeled or presented.

18 For the definition of "leased tangible capital asset", please refer to Section #7 of the Leasing Guideline.

19 Part of this analysis would fall under the Risk Assessment which is more fully set out in Section #6.

Guideline 9

Government requirements, which would not ordinarily be provided under sound feasibility analysis and where there is no alternate use or market for the leased real property is also indicative of a capital acquisition through an alternative financing method (e.g. lease). Where the Government may also exercise control or impose restrictions on the use of the facility, particularly any excess capacity, the substance of the agreement may be considered capital in nature.

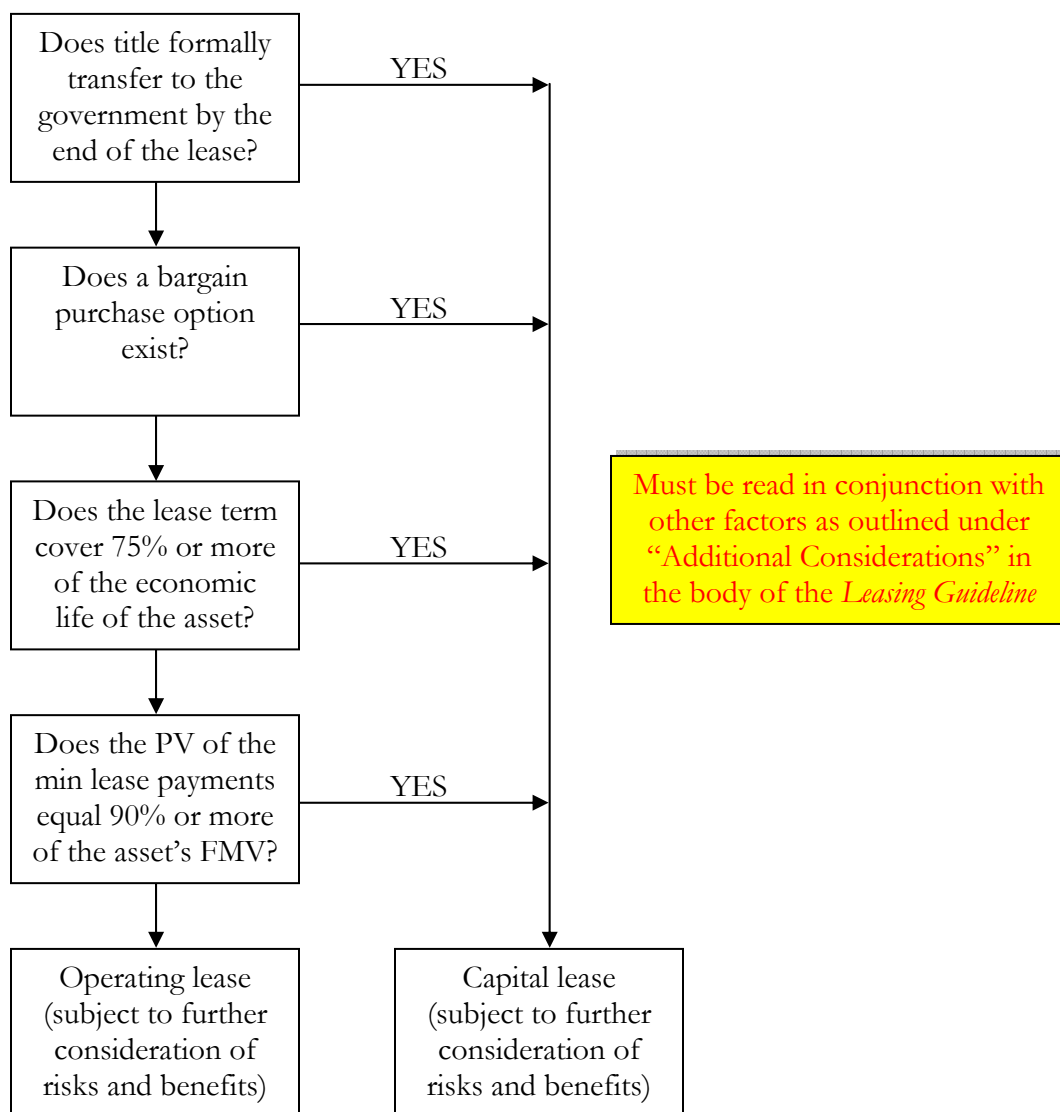
The Government, in an effort to meet its requirements, also may provide financial assistance to the lessor toward the cost of acquiring or constructing the facility through various avenues. Where this is the case or where the Government has provided guarantees in the event of default by the lessor, it may be viewed that the risks of ownership have transferred to the Government and it is operating to protect its beneficial rights to the leased real property.

Lease Classification: Summary of Criteria

Based on CICA Public Sector Guideline 2 “Leased Tangible Capital Assets” (April 2000)

The following criteria must be weighed in conjunction with the specific facts of each situation and the risks and benefits borne by each party to the lease agreement prior to making any conclusion with regard to the appropriate lease classification.

(Please refer to the Leasing Policy and Leasing Guidelines for further details.)



All such factors must be considered as part of any lease analysis, including the internal consistency of the factors and likely motives and expectations of both parties to the lease agreement.

Fiscal Considerations

Each financing alternative carries its own reporting requirements that are reflected in the Public Accounts. Therefore the fiscal implications under each scenario should also be considered in any analysis.

An operating lease does not confer significant risks or benefits to the GN and thus is treated in a similar manner as a rental agreement. Accordingly, the total annual lease payments should be appropriated and accounted for as operating expenditures (under Vote 1). Lease payments would then be reflected in the Public Accounts in the period to which they relate on an accrual basis.

Acquiring real property through direct purchase, however, requires a commitment of capital dollars and therefore should be reflected as capital expenditures (under Vote 2). Acquisition costs would then be reflected in the year of purchase and would directly increase the Net Debt of the GN. Amortization²⁰ would be charged annually to operations over the course of the asset's life.

Acquiring real property by way of a capital lease follows the same requirements and has a similar impact on Net Debt as a direct purchase (as outlined above). It is important to note that under a lease scenario Net Debt will be further impacted by the extent of any lease premium²¹. Operations also will be impacted by imputed interest expense over the lease term in addition to the annual amortization charge.

20 Amortization is the process of charging a portion of the cost of the leased tangible capital asset to operations annually over the period of expected use of the asset. This basis for amortization should be consistent with the GN's policy. For clarification, please refer to the Department of Finance.

21 This summary reflects the existing accounting standards in place for public sector entities as issued by the Public Sector Accounting Board of the Canadian Institute of Chartered Accountants.

Risk Assessment

To determine whether a lease agreement is operating or capital in nature, a thorough risk assessment is required. The following lists some of the risks which should be considered as part of this exercise. As the risks and benefits to the GN will depend on the facts of the situation, this list is not exhaustive.

- a) **Operating risk:** lack of obligation on the part of the owner to compensate the GN or provide alternative facilities in the event the facility does not perform to agreed standards means that the GN is assuming operating risk related to the facility.
- b) **Business risk:** provisions for significant future cost increases, or escalation clauses linking costs to indices (e.g. the Consumer Price Index) imply that the GN is assuming or sharing business risks related to the facility.
- c) **Construction risk:** if the GN bears the risk of cost overrun (e.g. through lease payments based on actual costs rather than a predetermined price for the facility), the GN bears construction risk.
- d) **Demand risk:** an obligation for the GN to pay for the full capacity of the facility even though expected demand does not materialize transfers demand risk to the GN.
- e) **Other potential risks:** other risks such environmental liabilities, obsolescence, or uninsured damage also may be transferred to the GN depending on the specific lease terms.

The following chart provides an example of risk assessment for a specific project.

TYPE OF RISK	DESCRIPTION	RISK ALLOCATION PROVIDED IN LEASE	
		GN: Tenant / Lessee	Landlord / Lessor
1. Construction Risk	<i>This relates to the risk of cost overrun during construction and the lease being based on actual rather than a predetermined project cost.</i>	Capital cost and rent is adjusted to reflect actual costs.	Landlord owns the building at the end of the lease period and bears the risk of major deterioration or depreciation of the facility.
2. Operating Risk	<i>This is the risk that a facility does not function properly. The lessor can mitigate the risk agreeing to provide alternative facilities, or compensating the tenant in the event of failure.</i>	Rent will not be abated due to obstruction related to repairs or maintenance provided landlord is not at fault. Alterations are subject to approval of the landlord and to be paid for by the GN.	Costs of making and keeping the facility compliant with energy codes are the responsibility of the landlord. Landlord is responsible to maintain structural condition of facility.
3. Business Risk	<i>This is the risk of, for example, future O&M cost increases. If O&M is specified at a fixed price, the lessor bears the risk, but if the lease provides for cost 'flow-through', the tenant bears the risk.</i>	Operating and maintenance costs as specified are either flow-through based on actual costs, or are indexed. Rate of interest is based on actual financing cost for loan portion.	Maintenance costs related to the building including acts of vandalism, costs covered by insurance, and capital costs. Return on equity financing is specified and fixed. Landlord is responsible for income taxes.
4. Demand Risk	<i>This is the risk that a facility leased in full cannot be fully utilized. Allowing the tenant to sub-let or use the space for non-designated purposes can mitigate the risk.</i>	Building cannot be sublet in whole or in part without prior consent of the landlord. Such consent cannot be reasonably withheld. Landlord may reduce land available to the tenant if this does not unreasonably affect the tenant.	GN has right to approve any proposed alternative use of space.