

**Interim Evaluation of the Structured Financing Facility  
Management Response  
May 18, 2005**

**General Comments**

The program's level of success has been lower than had been anticipated, especially with regard to the exploitation of domestic opportunities. The evaluation has determined that this is largely the result of design deficiencies in the program related to restrictions imposed by tax regulations. Meanwhile, the findings of the evaluation are generally positive as regards the management of the program.

Several of the recommendations go beyond the scope of the SFF program: promotion of free trade; revisions to tax regulations; implementation of performance bonds, promotion of innovation. This is legitimate given that the recommendations are linked to the SFF through the policy framework. Other recommendations call for improved program administration: better marketing to Canadian shipowners, better monitoring of SFF impacts on innovation. Finally, the evaluation calls attention to program deficiencies including the failure of credit insurance and the failure to provide adequate incentive to domestic shipowners.

**Recommendations and Management Responses**

**State of Shipbuilding in Canada and Worldwide**

1. *The Canadian government should increase pressure within international trade groups, such as WTO, OECD and NAFTA, to eliminate subsidies and protectionism in shipbuilding. In particular, the government should monitor US attempts to extend Jones Act provisions to smaller ships and yachts.*

**Management Response**

Agree.

**Follow-up Action:** The Marine Directorate will continue to send representatives to the OECD negotiations, and assist in the development of a negotiating mandate for Canada. The directorate will also continue to monitor other trade issues, including the Korean FTA and the EFTA (European FTA) and U.S. Jones Act developments.

**Timeframe:** On-going.

2. *The success of Australia and the Netherlands in building viable shipbuilding industries*

*should be examined in detail to determine lessons of value to developing the Canadian industry.*

**Management Response**

Agree. A key role of the SFF is to help Canadian yards exploit niche markets.

**Follow-up Action:** Initiate comparative case studies while monitoring Canadian success. Consider successful practices elsewhere that may have application in Canada in the context of the policy review.

**Timeframe:** In the current policy review cycle, this calendar year.

**Rationale and Relevance**

3. *SFF should be retained by Industry Canada as a non-repayable incentive to the Canadian shipbuilding industry.*

**Management Response**

Agree.

**Follow-up Action:** Develop a proposal for the renewal of the SFF.

**Timeframe:** In the current policy review cycle, this calendar year.

4. *Industry Canada should consider with the Department of Finance means of ensuring that the tax treatment of shipbuilding lessors is equivalent to that of lessors in road and rail.*

**Management Response**

Agree. Nevertheless, tax regulations are in the exclusive domain of the Department of Finance.

**Follow-up Action:** Assist industry in making representations to the Department of Finance and to the Minister of Industry.

**Timeframe:** On-going

5. *The benefits of the SFF to the industry should be enhanced by means of the changes to*

*the program's design and delivery recommended in this report.*

### **Management Response**

Agree.

**Follow-up Action:** Management is considering program improvements for a renewed SFF program to overcome current design deficiencies.

**Timeframe:** In the current policy review cycle, this calendar year.

### **Program Design and Delivery**

6. *Industry Canada should increase the awareness of SFF amongst Canadian fleet operators by making personal contact with the acquisition decision makers within each Canadian fleet. Non-members of the Canadian Shipowners Association should receive particular attention. The Department should share its market research on upcoming fleet acquisitions with the shipbuilding industry.*

### **Management Response**

Agree.

**Follow-up Action:** Greater emphasis will be placed on marketing the program directly to fleet operators.

**Timeframe:** On-going

7. *The term of SFF should be extended beyond five years (that is beyond 2006) for a possible two to three years, at a minimum by grandfathering contracts signed before the end of the current program period, to allow Canadian industry more time to increase its market share and develop a good set of reference customers.*

### **Management Response**

Agree.

**Follow-up Action:** Industry Canada is considering the proposal of a renewal of the SFF program which will allow action on projects considered during the current program period. Absent such a renewal, it may be possible to extend the SFF by one or two years for current projects.

**Timeframe:** In the current policy review cycle, this calendar year.

8. *The CIS and CIC components should be retained. Industry Canada and the Department of Finance should create procedures that will facilitate the application process and Industry Canada should communicate the benefit of these components better to the shipyards.*

**Management Response**

Partially agree. Credit insurance components (CIS and CIC), in their current form, have not proved practical. Better procedures are needed to make these components workable. Once a workable program is in place, shipyards and applicants can be made aware that these components are available.

**Follow-up Action:** Consideration of the integration of these components, with improved procedures, into a renewed SFF program.

**Timeframe:** In the current policy review cycle, this calendar year.

9. *SFF should be extended to all R&O work and to yachts.*

**Management Response**

Disagree that SFF should be extended to R&O. Canadian shipyards have locational advantages such that SFF incentives are not required in order to obtain repair and overhaul (R&O) contracts. Meanwhile, support for new build opportunities is important so that yards can remain up-to-date and offer R&O services.

The SFF is already available to support the building of yachts for commercial usage.

**Follow-up Action:** Extension of SFF to yachts for personal usage will be considered in the context of a renewal of the program.

**Timeframe:** In the current policy review cycle, this calendar year.

10. *The current practice of determining incrementality by requiring foreign quotes should be replaced by a certification process with the ship buyer.*

### **Management Response**

Partially agree. The ship buyer must make the case that SFF funding is required for the project to proceed at the Canadian yard. Foreign quotes are strong evidence but not necessarily the only possible evidence for making this case.

11. *Industry Canada should communicate to the shipbuilding industry that early discharge of loans receiving SFF support is not allowed. Industry Canada should also review with the Department of Finance means for providing an incentive to cash purchasers of ships who are not eligible for SFF support. Possible incentives for domestic cash buyers would be to increase the ACCA amortization rate or to allow amortization during the ship's construction.*

### **Management Response**

Agree. The integrity of the program requires that a *bona fida* loan be in place. Applicants need to be aware of this. Meanwhile, changes to amortization are in the exclusive domain of the Department of Finance. Finally, such changes would not address the question as to how to provide an incentive to foreign buyers who pay cash.

**Follow-up Action:** Assist industry in making representations to the Department of Finance and to the Minister of Industry.

**Timeframe:** On-going

12. *Industry Canada should introduce new measures such as orders for new types of vessels to improve the assessment of innovation in Canadian shipyards.*

### **Management Response**

Agree. However, the lack of innovativeness of a shipbuilding project does not disqualify a project from support.

**Follow-up Action:** SFF's impact on innovation (new types of vessels) will be tracked. As part of the policy review, we will also investigate the benefits of an SFF that is more targeted on innovation and skills upgrading.

**Timeframe:** In the current policy review cycle, this calendar year.

### **Program Success**

13. *The government of Canada and relevant provinces, along with Crown Corporations,*

*such as BC Ferries and Marine Atlantic, should embark on a coordinated, multiyear fleet replacement program, with Canadian shipyards getting preferential treatment to win contracts.*

#### **Management Response**

Agree. However, the Canadian shipbuilding policy requires that a competitive environment exist among Canadian shipbuilders so that public shipowners are not unduly disadvantaged by the policy. In some cases, SFF support may be justified to keep the work in Canada at a reasonable price to the buyer.

**Follow-up Action:** Discuss with other stakeholders, and especially Department of National Defence and Canadian Coast Guard, how to co-ordinate government procurement so as to maximize benefit to the industry while at the same time enabling industry to meet government requirements. Included here is an effort to level out demand and identify and overcome industry capacity (and productivity) gaps.

**Timeframe:** This discussion is part of the current agenda aimed at finding a way to transform the shipbuilding industry.

14. *Industry Canada should work with the Department of Finance to allow ACCA and SFF to be applied simultaneously.*

#### **Management Response**

Agree. Nevertheless, tax regulations are in the exclusive domain of the Department of Finance.

**Follow-up Action:** Assist industry in making representations to the Department of Finance and to the Minister of Industry.

**Timeframe:** On-going

15. *Industry Canada together with the Department of Finance should consider strengthening the balance sheets of Canadian shipyards by providing guarantee performance bonds, in much the same way that that Investment Quebec does.*

### **Management Response**

Disagree. For the federal government, in relation to exports, the guarantee of contract performance falls within the realm of the Canadian Commercial Corporation (CCC). SFF support is limited to assuring performance on loans (credit insurance).

The consideration of performance bonds for domestic sales lies outside the scope of the SFF.

16. *Industry Canada should review with EDC the provision in the shipbuilding policy that allows EDC to match financing terms when competitors for a project transgress OECD guidelines to ensure that applicants for SFF can bid with competitive support.*

### **Management Response**

Agree.

**Follow-up Action:** Industry Canada will continue to work closely with Export Development Canada (EDC) on all projects in which they are mutually involved.

**Timeframe:** On-going

17. *The Marine and Ocean Industry Technology Roadmap (TRM) should be followed up to determine its impact on the Canadian shipbuilding industry and propose actions necessary to improve the level of innovation in the industry.*

### **Management Response**

Agree. The Marine Directorate, through a working group, analyzed the Technology Road Map in terms of the objectives of the Ocean Action Plan. Several shipbuilding initiatives were identified.

**Follow-up Action:** Participate in the working group in Phase II of the Ocean Action Plan. Consider possible actions to improve the level of innovation in the industry in the context of the current policy review.

**Timeframe:** In the current policy review cycle, this calendar year

18. *Industry Canada should make Canadian shipyards and labour organizations aware that they are losing commercial work because of their reputation for late deliveries and cost overruns.*

### **Management Response**

Agree.

**Follow-up Action:** The Shipbuilding and Industrial Marine Advisory Committee (SIMAC) is the forum in which this issue can be discussed.

**Timeframe:** A meeting of SIMAC is tentatively scheduled for the fall (2005).