Report: COR-FSD-20-11

Region of Waterloo

Corporate Services

Financial Services and Development Financing

To: Chair Sean Strickland and Members of Council

Date: April 14, 2020 **File Code:** A01-01(A)

Subject: Annual Adequacy of Regional Development Charge Collections Review

Recommendation:

For Information

Summary:

This report presents analysis and commentary relating to the Region’s development charge (RDC) collections/reserve fund balances to assist in determining the adequacy of the RDC rates established under the current Development Charge By-law. Details relating to the RDC collections and appropriations can be found in the annual RDC Transaction Report (COR-FSD-20-05 dated March 24, 2020).

While the 2019 closing position of the consolidated RDC reserve is slightly over $60 million, there remains inherent cash flow risks to the RDC Reserve funds from economic and legislative influences that need to be mitigated. The increasing need to issue growth-related debt to finance the cost of growth-related infrastructure also exposes the Region to development charge revenue risk, in that the Region will need to meet the contractual obligation to pay debt servicing costs from an uncertain, and potentially inadequate, development charge revenue stream.

The Region’s Development Charge By-law 19-037 came into force on August 1, 2019 and expires on July 31st, 2024. The supporting background study utilized information from several recently completed master plans. Council implemented the maximum calculated Development Charges Rates as set out in the background study and those rates have been in effect since August 1, 2019. St. John’s Kilmarnock School has filed

and appeal of the by-law with the LPAT, the timing for resolution of which, is uncertain at this time. The Province has introduced legislation that amends the Development Charges Act (DCA) with some amendments coming into force on Jan 1, 2020 and others that have yet to be proclaimed and will come into force at a later date.

The Region's Development Charge By-law was recently updated and the maximum calculated rates imposed. Given the uncertainty surrounding the appeal of the by-law and further legislative amendments to the DCA likely coming into force in 2020, staff will continue to monitor RDC collections, capital project costs and the legislative environment, with no specific action required from Council at this time. That being said, Council may want to consider future amendments to the RDC By-law to align the wording of certain sections of the by-law with the amendments set out in the DCA once they have all come into force (potentially late 2020 or early 2021). Staff will continue to monitor and update Council as more information becomes available.

Report:

Development Charge Reserve Funds

Contributions to the RDC Reserve funds result from RDC collections as well as exemptions, discounts and community housing grants funded from Regional Sources and interest allocations. Appropriations from the RDC reserves are used to fund eligible growth-related capital projects, existing debt servicing costs and to recover funds for RDC eligible projects that were previously funded from tax levy or user rate sources. A five-year continuity of the consolidated RDC Reserve Fund is set out in the following table:

Table 1

Five Year Continuity of RDC Reserve Fund ($ Thousands)

	2015	**2016**	**2017**	**2018**	**2019**
Opening balance	$66,269	$52,327	$66,409	$45,383	$36,808
Add: contributions	45,831	82,070	58,618	57,706	90,210
Less: appropriations	(59,773)	(67,989)	(79,643)	(66,281)	(66,788)
Closing balance	$52,327	$66,409	$45,383	$36,808	$60,229

Although the position of the consolidated RDC Reserve Fund remains positive and has increased over the ending 2018 position, it should be noted that $224 million in growth related debentures has been issued across various RDC eligible services resulting in an increasing share of annual RDC collections allocated to fund existing debt servicing costs. Along with the increasing reliance on growth-related debt, there are inherent economic and legislative risks, among others, outlined in the following sections that could potentially impact the cash flow of the RDC reserves.

RDC Reserves - Risk Analysis and Mitigation Measures

A) Financing of Growth-Related Infrastructure

The timing of certain growth related projects relative to expected RDC collections will necessitate the issuance of additional growth-related debt. This is particularly evident for water and wastewater infrastructure where the additional capacity must be available well in advance of the issuance of building permits and the corresponding collection of development charges. Over the 2013 to 2019 period, approximately $224 million of growth-related debt has been issued to finance the construction of growth-related infrastructure, resulting in annual debt servicing costs of $14.5 million (see Appendix A).

The Region's 2020-2029 Capital Plan contemplates additional growth-related debt requirements of approximately $400 million. The need for additional growth-related debt exposes the Region to development charge revenue risk, in that the Region will need to meet the contractual obligation to pay debt servicing costs from an uncertain, and potentially inadequate, development charge revenue stream. This is particularly evident in Water, Wastewater and Transportation where an increasing share of RDC collections are required to fund debt servicing costs. Appendix B shows the projected percentage of annual RDC collections required to fund existing debt servicing costs for Water, Wastewater and Transportation as set out in the 2020-2029 Capital Plan.

The development charge rates currently in effect were calculated using estimated costs in the 2019-2028 Capital Plan. As projects move into detailed design, amendments to the estimated costs may be required for some projects. Projects that require more RDC funding than originally contemplated in the calculation of the rates may require the issuance of additional growth-related debt as the additional costs will be recovered from future RDC rates.

Commissioners, directors and senior technical staff from Corporate Services, Transportation and Environmental Services and Planning, Development and Legislative Services continue to review and monitor the 10 - year forecasts for the development charge reserves with a view to manage the levels of debt servicing costs in relation to annual collections. The percentage of RDC collections allocated to fund growth-related debt servicing costs will be monitored as a Key Performance Indicator under section 5.4 of the Strategic Plan to "Ensure the Region provides value for money and long term financial sustainability". Staff will continue to monitor the growth-related infrastructure financing requirements and report to Council through Periodic Financial Reports and the annual budget process

B) Economic Cycles

Economic cycles and the timing of actual development relative to the growth plan also presents an inherent risk to the level of RDC collections in a given year. The economic impacts of the COVID-19 Pandemic and the related impacts on development are difficult to predict at this time. It is expected that the global economic slowdown will impact growth in Waterloo Region which in turn will impact RDC collections over the near term. The extent is difficult to ascertain at this point. The influx of building permits in advance of the core area expiry in February 2019 and the Region's DC by-law expiry in July of 2019 will also likely result in a decrease in the number of permits issued and the related development charges collected throughout 2020.

As set out in Report COR-FSD-17-33 dated November 22, 2017, Council approved a 10 - year funding strategy to fund downtown core RDC exemptions prior to their expiry in February 2019. Accordingly, $4.1 million will be transferred annually from user rate and tax levy sources to the RDC reserves. Staff will continue to assess the need and timing of growth-related projects within the context of current economic conditions and anticipated development in the Region and report to Council as required.

C) Legislative Changes to the DCA

As set out in report COR-FSD-20-10 dated January 14, 2020, recent legislative changes to the DCA have changed when RDCs are determined and collected. Development charges have historically been assessed and collected at building permit issuance. Under the revised legislation, development charges are now assessed at site plan, zone change or building permit issuance and frozen for up to two years. Deferred payment plans have been introduced in 2020 for purpose-built rental and institutional development (5 years) and non-profit housing (20 years). Although several unknowns remain, staff have estimated the impact of delayed payment regimes for rental, non-profit housing and institutional developments to be in the range of $40-$50 million over the 2020-2029 period with the majority of the impact occurring in the first five years. Freezing the calculation of DCs for a particular development at the later of site plan application date or zoning application date will also impact development charge collections as DCs have historically been assessed at the building permit stage. This means that certain developments will not be subject to RDC rate increases that would occur through a RDC By-law update. The impact of this amendment is difficult to estimate at this point

As a mitigating factor, amendments to the DCA provide municipalities with the ability to charge interest from the time that the DC is assessed to the time that the DC is paid, including those developments subject to the deferral plans. Staff from the Region and area municipalities are participating in a working group to implement the necessary administrative processes necessitated by the amendments to the DCA. The group is currently assessing options with respect to interest rate policies with a view to align the rates, calculations and policies where feasible. Staff from this group will report back to their respective Councils with recommended interest rate policies for development charge by-laws in the Spring.

D) Development Charge By-law Appeal – St. John's Kilmarnock School

The Region's new Development Charge by-law was approved by Council on June 26, 2019, and new RDC rates came into effect on August 1, 2019. St. John's – Kilmarnock School has filed an appeal of the by-law with the Local Planning Appeal Tribunal (LPAT). Should the LPAT choose to reduce or eliminate the quantum of the development charges, the revenue differential must be refunded with prescribed interest. The Region's RDC By-law is in full force and effect including the new rates unless and until the LPAT orders otherwise. The case management conference, originally scheduled for March 18, has been adjourned until further notice due to the COVID-19 Pandemic. Staff and external counsel will defend the appeal and update Council as required.

Concluding Comments

The Region's Development Charge By-law was recently updated and the maximum calculated rates imposed. Given the uncertainty surrounding the appeal of the by-law and further legislative amendments to the DCA likely coming into force in 2020, staff will continue to monitor RDC collections, capital project costs and the legislative environment, with no specific action required from Council at this time. That being said, Council may want to consider future amendments to the RDC By-law to align the wording of certain sections of the by-law with the amendments set out in the DCA once they have all come into force (potentially late 2020 or early 2021). Staff will continue to monitor and update Council as more information becomes available.

Corporate Strategic Plan:

This report supports strategic objectives found in the Corporate Strategic Plan, and particularly section 5.4 Ensure the Region provides value for money and long term financial sustainability under Focus Area 5, Responsive and Engaging Public Service.

Financial Implications:

The Regional Development Charge is a significant component of financing for the Region's capital program. The Region's approved 2020-2029 Capital Program requires just under $1.0 billion of RDC funding to fund the projected growth-related capital costs for that period. The timing of certain growth projects relative to expected development charge collections will necessitate the issuance of additional growth-related debt estimated at $400 million over the next ten years. Staff will continue to assess the need and timing of growth-related projects within the context of current economic conditions and anticipated development in the Region and report to Council as required through the Periodic Financial Reports and the annual budget process.

Other Department Consultations/Concurrence:

NIL

Attachments

Appendix A – Total Growth-Related Debt Issued to Date and 2019 Debt Servicing Costs

Appendix B – 2020-2029 Capital Plan - % of Annual RDC Collections Required to Fund Debt Servicing Costs for Water, Wastewater and Transportation

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Approved By: Craig Dyer, Commissioner, Corporate Services/Chief Financial Officer

Appendix A Total Growth-Related Debt Issued to Date and 2019 Debt Servicing Costs ($000's)

Service	Total Growth Related Debt Issued to Date	2019 Debt Servicing Costs	Project Description
Wastewater	$118,865	$8,121	Wastewater Treatment Plant upgrades for Kitchener, Waterloo, Galt and Ayr. Influent channel twinning in Kitchener.
Transit	63,281	5,142	Stage 1 LRT, King Victoria Transit Hub, Northfield Drive Operations & Maintenance Facility, Fairview Mall terminal,
Transportation	30,610	420	River Rd., Homer Watson Blvd., Northfield Dr., Franklin Blvd., South Boundary Rd.
Police	2,141	138	Property Acquisition
Paramedic	2,774	205	EMS Stations: HQ/North Fleet Centre, Breslau and Kitchener
Airport	6,462	424	Property Acquisition
Library	172	20	Library Headquarters Expansion
Total All Services	**$224,305**	**$14,470**	

Appendix B 2020-2029 Capital Plan - % of Annual RDC Collections Required to Fund Debt Servicing Costs