Report: COR-FSD-15-17

Region of Waterloo

Corporate Services

Financial Services & Development Financing

To: Chair Sean Strickland and Members of the Administration & Finance Committee

Date: October 27, 2015 **File Code:** F27-50

Subject: Annual Adequacy of Regional Development Charge Collections Review

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Recommendation:

For Information

Summary:

The Annual Adequacy of Regional Development Charge (RDC) Collections Review presents analysis and commentary relating to the Region's development charge collections/reserve funds and potential legislative changes to assist Council in determining the sufficiency of the development charge rates established under the current Development Charge By-law. The Region's current RDC By-law came into effect on August 1, 2014 and is set to expire on July 31, 2019 unless repealed earlier. Development charge revenue during the first year under RDC By-law 14-046 was lower than originally anticipated for a number of reasons including statutory RDC exemptions, discounted rates and the type and timing of development.

In response, a working group comprised of the CAO, Commissioners, Directors and Managers from Transportation and Environmental Services, Corporate Services, and Planning, Development and Legislative Services met on several occasions this year to develop strategies related to financing the growth-related portion of capital projects (development financing) for inclusion in the 2016-2025 Capital Plans. A combination of spending adjustments, interim financing and long term borrowing will be required to ensure that the RDC Reserves maintain adequate balances.

Through Bill 73, the Province has introduced proposed amendments to the Development Charges Act (DCA) (which could increase the amount of development charges to be collected) and to the Planning Act. Bill 73 recently received second

reading in the Legislature and has been referred to the Standing Committee on Social Policy. It is anticipated that the Bill will be passed in late 2015 and that the associated regulations will be approved in early 2016. Upon approval of the Act and regulations, staff will report back to Council with analysis, options and a recommended course of action.

Report:

Background

The Development Charges Act (DCA) provides the legislative authority and framework for municipalities to impose development charges upon the development of land and sets out the associated processes, procedures and reporting requirements. While the DCA provides municipalities with the authority to recover growth-related infrastructure costs from new development, the exclusion of certain municipal services and the methodology prescribed for calculating the charge constrain the ability to adequately recover the overall cost to support growth.

The purpose of the Regional Development Charge (RDC) is to recover, to the greatest extent possible, growth-related capital costs from those segments of the community (namely residential and non-residential development) which give rise to the need for additional growth-related capital works.

The DCA prescribes how the development charges are to be calculated. The RDC rates are established by projecting growth, determining the increase in capital infrastructure necessary to service that growth (taking into account service level standard constraints and existing excess capacity), estimating the costs of that infrastructure, and determining the unit charges which may be recovered from development to provide the necessary revenue to finance growth-related expenditures.

The Region prepares a Development Charges Background Study which incorporates all these principles in order to calculate the maximum allowable RDC rate under the DC Act. There is an opportunity for public input and review of the Background Study and draft By-law. Council then approves the By-law to collect development charges.

The Region’s current RDC By-law came into effect on August 1, 2014 and is set to expire on July 31, 2019 unless repealed earlier. Appendix A lists the services for which the Region collects development charges and a 5 year history of the RDC reserve fund balances.

Development charges are collected by the area municipalities on behalf of the Region at the time of issuance of a building permit. The funds are remitted to the Region on a monthly basis and are allocated to service-specific reserve funds, which in turn are used to finance approved capital expansion projects in the Regional services areas listed above.

Regional Development Charges – Annual Reporting to Council

Council will receive the following two annual reports related to Development Charges:

1. Annual Development Charge Transaction Report – This report presents the annual summary of development charge transactions for the prior fiscal year as required by the Development Charges Act. A copy is provided to the Ministry of Municipal Affairs and Housing and interested stakeholders. A copy is also posted on the Region's website. This report is typically presented in the spring.

2. Annual Adequacy of Development Charge Collections Review – This report will present analysis and updates relating to the development charge reserves and potential legislative changes to assist Council in determining the sufficiency of the development charge rates established under the prevailing Development Charge By-law. As part of the approval of the current RDC By-law through report F-14-088 on June 27, 2014 Council passed the following resolution:

   > "That having reviewed the development charge rates and determined the rates to be included in the Development Charges by-law, direct staff to monitor the development charge collections and capital program expenditures and report back annually on any shortfalls which may result to assist Council in determining the sufficiency of the rates established under the Development Charge by-law and the appropriateness of re-opening the by-law at that time, with the first report not later than fall 2015."

This report is the first such update to Council with subsequent updates to be presented to Council in the spring of 2016 and annually thereafter. Presenting this report annually in the spring will be based on information consistent with the Region's annual financial statements.

Development Charge Revenue

Development charge revenue is comprised of RDC collections from residential and non-residential development as well as funding from Regional sources to offset discretionary exemptions and discounts. The DCA requires that any shortfall in development charge revenue resulting from development charge exemptions and discounts approved by Council be funded from sources other than higher charges on other development. The following such exemptions are provided in the RDC By-law:

1) Downtown core exemption: provided in any area municipality which enacts a similar exemption. Currently, full downtown core exemptions exist in Kitchener and Cambridge. All Regional downtown core exemptions will expire on February 28, 2019.

2) Remediated Brownfield Site: an RDC exemption is provided in the amount of the eligible remediation costs to a maximum of the RDC payable.

3) Farming, community housing and public hospitals.

4) Since August 1, 2014 the Region has discounted the industrial RDC by 50%, in order to encourage new industrial development.

The total cost of development charge exemptions and discounts is financed from user rate reserve funds and property tax reserve funds/levies. The development charge collections and funded exemptions/discounts from Aug 1, 2014 to July 31, 2015 are shown in the table below:

Development Charge Collections & Funded Exemptions/Discounts			
Aug 1, 2014 to Jul 31, 2015			
($000's)	**Residential**	**Non-Residential**	**TOTAL**
RDCs Collected	$27,934	$7,884	$35,764
Industrial Discount	-	563	563
Downtown Core	52	43	95
Brownfield	993	-	993
Total	$28,979	$8,489	$37,468
% of Total	77%	23%	100%

Development charge collections and funded exemptions during the first year under RDC By-law 14-046 (August 1, 2014 to July 31, 2015) totaled $37.5 million. Of the total revenue, $29 million was attributable to residential development and $8.5 million was for non-residential development. The $1.7 million of exemptions was funded from the tax levy ($1.0 million) and user rates ($ 0.7 million).

Based on the maximum permissible rate calculated in the Background Study, RDC revenue in the first year of the by-law was estimated to be approximately $66 million. However, in order to reduce the magnitude of the increase in RDC rates, Council approved a 10% reduction in the capital costs related to Roads, Water and Wastewater.

Accordingly, the approved RDC rate was 9.7% lower than the maximum permissible rate, resulting in an effective revenue reduction of approximately $7 million. Actual RDC revenue is lower than anticipated due to a number of factors including:

- The Region's current RDC By-law came into effect on August 1, 2014. In anticipation of an RDC rate increase, a significant number of building permit applications were received in the weeks leading up to the expiry of the former RDC by-law on July 31, 2014. The total value of RDC collections and funded exemptions/discounts in July 2014 alone was almost $19 million, where under the previous by-law, typical RDC collections and funded exemptions/discounts in a given month would have averaged approximately $2-4 million.
- The type of development that has proceeded over the last year was different than had been contemplated with fewer apartments and more single family units.
- Although development activity remains strong, the rate of population growth has been marginally lower than was expected.
- The DC Act provides statutory exemptions for development related to the creation of additional dwelling units in residential buildings, the enlargement of the gross floor area of existing industrial buildings up to 50% of the existing gross floor area, and development on land owned by municipal, provincial and federal governments and local boards. The Region does not collect RDC's on these developments nor are these exemptions required to be funded from other sources as the non - statutory exemptions (i.e. Downtown Core and Brownfield) are. These exemptions can fluctuate significantly year over year and have averaged roughly $5-$6 million annually over the past 5 years.

Building Permit Activity and Development Charge Collections

Development charges, where applicable, are collected upon the issuance of building permits. It should be noted that there are several situations where the issuance of a building permit does not result in the collection of a development charge due to statutory exemptions, redevelopment allowances and the type of building permit issued (i.e. RDC's are only collected on the first permit issued). Also, in some cases, there can be a time lag between building permit application and issuance which can result in the development charge collections and building permit activity being reported in different periods. Consequently, increases in building permit activity in a given period, does not necessarily translate into increased development charge revenue over the same period. For example, Report # PDL-CPL-15-47 "Building Permit Activity – January to June 2015 presented to Council September 15, 2015 included the following high value developments:

- $16 million for an addition to the Applied Health Science building – University of Waterloo – RDC's were collected in November 2014.

- $15 million for the interior finish of the Breithaupt Block (Google) – RDC's are not collected on interior finish permits
- $5.4 million for a shell only to Westco Cambridge Inc. (FedEx) - RDC's were collected in November 2014
- $56 million for the 25-Storey ICON 330 mixed-use building with 624 units located at 330 Phillip Street - RDC's collected on 597 Units in July 2014 (redevelopment allowance applied to the other 27 Units)
- $23.9 million for the 14-storey Trio on Belmont located at 460 Belmont Ave West with 172 Units – No RDC's collected due to redevelopment allowance
- $6.2 million for a women's shelter and administration offices – RDC's were collected in June 2015

Bill 73, Smart Growth for Our Communities Act, 2015 Update

Through Bill 73, the Province has introduced proposed amendments to the DCA which could increase the amount of development charges to be collected to offset the cost of growth related capital works and also contains changes to the Planning Act that were previously supported by Council. According to the Environmental Bill of Rights registry, the amendments proposed by Bill 73 to the DCA, if passed, would:

- Enhance funding for municipal transit systems;
- Enhance transparency and accountability regarding payment of development charges (DCs) and additional fees;
- Identify any services which are ineligible for collection of development charges through regulation;
- Require municipalities to examine the application of varying development charges within different areas of a municipality; and
- Enhance the reporting requirements for development charges.

Earlier this year the Province formed several working groups of stakeholders (developers, municipal representatives) to review certain proposed amendments to the DCA. Chair Seiling and Region of Waterloo staff were active participants in this process.

Regional staff previously reported to Council on Bill 73 and the proposed amendments to the DCA through Report COR-FSD-15-07 in March 2015 and Report COR-FSD-15-14, PDL-LEG-15-49 in August 2015. Bill 73 recently received second reading in the Legislature and has been referred to the Standing Committee on Social Policy. It is anticipated that the Bill will be passed by the end of 2015 with regulations to follow early in 2016. Provincial staff has indicated that amending the DCA is a key government priority.

Financing of Growth-Related Capital Projects

A working group comprised of the CAO, Commissioners, Directors and Managers from Transportation and Environmental Services, Corporate Services, and Planning, Development and Legislative Services has met on several occasions to discuss the financing of growth related infrastructure in the Region of Waterloo. The group's discussions to this point have focused on the following:

- Mitigating potential shortfalls in development collections should RDC collections be lower than anticipated as discussed above
- Proper alignment of the timing of the capital plan with anticipated growth
- Ensuring that the Regional DC reserves maintain adequate balances
- Approach to debt financing major infrastructure projects

The group has developed and incorporated strategies for financing certain major infrastructure projects into the 2016-2025 Draft Capital Plan. A combination of spending adjustments, interim financing and long term borrowing will be required to ensure that the RDC Reserves maintain adequate balances. Full details will be provided to Budget Committee at its meeting on November 18, 2015.

Rate Sufficiency

The Region's current RDC By-law is set to expire on July 31, 2019 unless repealed earlier. It is anticipated that Bill 73, Smart Growth for Our Communities Act, 2015 and associated regulations will be passed by the end of 2015 or early 2016. Through Bill 73, the Province has introduced proposed amendments to the DCA which could increase the amount of development charges to be collected under subsequent RDC By-laws. Accordingly staff is not recommending any action be taken until the Bill and regulations come into effect. Upon approval of the Act and regulations, staff will report back to Council with analysis, options and a recommended approach.

Corporate Strategic Plan:

This report supports strategic objectives found in the Corporate Strategic Plan, and particularly Focus Area 1.2: Plan for and provide the infrastructure and services necessary to create the foundation for economic success.

Financial Implications:

The Regional Development Charge is a significant component of financing the Region's capital program. Over the period of the By-law from 2014-2018, it is anticipated that approximately $0.5 billion of RDC funding is required to fund the projected growth related capital costs for that period. While development charge funding is significant, Regional taxpayers contribute a substantial amount toward the growth related capital costs. Projections indicate that the Region will be required to issue debentures to fund certain growth-related capital costs in the 2016-2025 capital budget and forecast in order to allow major projects to proceed to construction, as certain RDC reserve fund balances are expected to be insufficient to fund the growth-related portion of the projects.

Other Department Consultations/Concurrence:

Input was provided by Planning, Development and Legislative Services staff.

Attachments

Appendix A - Development Charge Reserve Funds Closing Balances 2010-2014

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Appendix A

Development Charge Reserve Funds - Closing Balances 2010-2014

($000's)	2010	2011	2012	2013	2014
Transportation	64,672	58,852	42,086	37,521	38,088
Water & Wastewater*	23,430	6,148	(18,638)	22,815	30,470
Airport	366	(2,827)	(2,523)	(2,158)	(1,444)
EMS	394	96	(158)	(205)	81
General Government	1,243	425	(302)	(697)	(1,245)
Library	123	133	108	75	59
Operations	787	1,214	1,548	1,901	2,436
Police	1,129	942	(1,236)	(374)	89
Transit	5,143	3,414	777	(2,553)	(2,264)
Total RDC Reserves	**97,286**	**68,396**	**21,662**	**56,325**	**66,269**

*$93 million in debentures have been issued for growth related Wastewater projects. The annual debt servicing costs ($7.1 million in the 2015 Budget) are funded from the Wastewater RDC Reserve Fund.