TO:	GENERAL COMMITTEE
SUBJECT:	DEVELOPMENT CHARGE INTEREST – BILL 108
WARD:	ALL
PREPARED BY AND KEY CONTACT:	M. VILLENEUVE, SUPERVISOR OF DEVELOPMENT CHARGES, EXT. 4503 J. COWLES, SENIOR MANAGER CORPORATE FINANCE AND INVESTMENT, EXT. 5347
SUBMITTED BY:	C. MILLAR, DIRECTOR OF FINANCE AND TREASURER, EXT. 5130
GENERAL MANAGER APPROVAL:	D. MCALPINE, GENERAL MANAGER OF COMMUNITY AND CORPORATE SERVICES
CHIEF ADMINISTRATIVE OFFICER APPROVAL:	M. PROWSE, CHIEF ADMINISTRATIVE OFFICER

RECOMMENDED MOTION

1. That the City authorize the following for the new mandatory deferral and instalment payments for non-profit housing developments in accordance with Section 26.1 (7) of the *Development Charges Act*:

   a) Interest charges be waived during the first five years of the loan; and

   b) Beginning on the date that the sixth instalment is due, interest charges be applied to development charges outstanding at a rate established by the City's Weighted Average Cost of Capital, as determined by the Director of Finance and be fixed for five year increments for the remaining duration of the loan.

2. That the City authorize the following for the new mandatory deferral and instalment payments for rental housing that is not non-profit housing and for institutional developments in accordance with Section 26.1 (7) of the *Development Charges Act*:

   a) Interest charges be applied to development charges outstanding, at a rate fixed for the duration of the loan and established by the City's Weighted Average Cost of Capital on the date that the first instalment is due and as determined by the Director of Finance.

3. That the City authorize an interest charge based on the City's Weighted Average Cost of Capital as determined by the Director of Finance for the new "frozen" development charges fixed from the date of the Site Plan or Rezoning application as the case may be and to the date of payment in accordance with Section 26.2 (3) of the *Development Charges Act*.

PURPOSE & BACKGROUND

Report Overview

4. The purpose of this report is to update Council with respect to the sections of Bill 108 that were proclaimed in December of 2019 and have come into force January 1, 2020.

Bills 108 and 138

5. On May 2, 2019, the Province introduced Bill 108 “More Homes, More Choice Act, 2019”, an Act to amend various statutes with respect to housing, other development and various other matters. The Bill proposed a number of significant changes to the Development Charges Act (DCA) and the Planning Act. The Bill was amended by the Standing Committee on May 29, 2019 and received royal assent June 6, 2019.

6. On November 6, 2019, the Province introduced Bill 138 “Plan to Build Ontario Together Act, 2019”, an Act to implement Budget measures and to enact, amend and repeal various statutes. Among other things, the Bill modified some of the articles in Bill 108, was amended by the Standing Committee on November 27, 2019 and received royal assent on December 10, 2019.

7. The predominant impacts of the provisions that came into force January 1, 2020 after being proclaimed December 10, 2019 are:

   a) Payment in Instalments:

      (1) not-for-profit rental housing developments will pay their development charges (DC) in 21 equal annual payments, while other than not-for-profit rental housing and institutional developments will pay their DCs in 6 equal annual payments commencing on the earlier of the date of the issuance of an occupancy permit or the date the building is first occupied.

   b) When DC Amount is Determined:

      (1) the DC rate for all developments will be determined based on the charge in effect on the day of application for site plan or zoning amendment. In cases where there are no such applications required, the rate will be based on the charge in effect on the day of the building permit issuance.

8. The changes listed above are a summary of matters related to development charges and are not an exhaustive list of all changes resulting from Bills 108 and 138. Not all changes have been proclaimed.

9. A summary of the legislative changes (proclaimed and not proclaimed) can be found in Appendix “A”.

ANALYSIS

10. On December 16, 2019, the City became aware that items listed in 7 a) were proclaimed and due to take effect January 1, 2020. As a result, some administrative matters require resolution.

   a) Interest on Deferred DC Receipts:

      i. The previous Development Charges regime required developments to pay all development charges prior to the issuance of a building permit. The new system allows certain developments to pay their development charges over 5 or 20 years from the date the building is occupied.

ii. The City funds a substantial amount of infrastructure required to be constructed prior to the incoming growth. With this legislative change, the delay in cash flow from these incoming developments will represent a higher financial risk to the City's cash position.

iii. The new legislation provides that municipalities may charge interest on such deferred development charges. The province has not prescribed a maximum interest rate but has reserved the right to do so. The amount of interest at this time is fully at the discretion of each individual municipality.

iv. Council's strategic plan includes the promotion of more affordable housing options. In setting an interest rate, the City should consider a balance between this strategic objective through low interest rates on deferred development charges and the City's financial requirements for investing in growth.

v. In conjunction with the City's Community Improvement Plan, which promotes and incentivises affordable housing options, the staff recommendation includes an interest free portion for the first 5 years of the 20 years of deferred payments by non-profit housing.

vi. To finance these changes, the City has to secure funding from various sources including internal reserves and long and short term debt. When using internal reserves, the City forgoes the benefit of earning interest on those funds. When using debt, the City's credit rating determines lending risk and drives the minimum interest rate charged by lenders. Both the loss of benefit of earning investment income and the interest rate charged by lenders yield a weighted average interest rate, referred to as the weighted average cost of capital (WACC). The benefit of WACC is that it is a combination of both internal and external factors, is unique to each entity, and captures the true cost of dedicating funds to any particular endeavour. At the end of 2019, the WACC sat at 4.78%.

vii. There is a financial risk of non-collection of payments given their long term nature, and the potential of future ownership changes. Loans of this nature would normally be secured by a letter of credit or an agreement registered on title of the property. However, the Province has not issued any regulations or guidance with respect to the posting of securities.

viii. At this time, staff are not making a recommendation to require security, as this would work against Council's strategic plan to increase affordable housing options. The deferral plans will be monitored and will be addressed should non-payment become an issue.

b) <u>**Interest on Freezing of DC rates:**</u>

i. The previous Development Charges regime required developers to pay the DC rates in effect at the time of the issuance of a Building Permit. The new system sets the rate of DC at the time of Site Plan Application or Zoning Amendment which is much earlier than when the construction will actually begin or when the amounts become due at Building Permit issuance.

ii. The freezing of rates from when an application is made to when the payment is due, will produce a shortfall in the amounts needed to cover growth related costs. Development charges are indexed each year in order to keep up to inflation. Additionally, a new Development Charge Study is required every 5 years in order to re-evaluate the rates in question. The Province has established a two year time limit for these rate freezes.

iii. The City considers an application of a Site Plan or Zoning Amendment to be made at the time that the submitted application is deemed to be complete.

iv. The new legislation allows municipalities to charge interest on the development charges to mitigate the additional costs associated with the rate freeze. The Province has not prescribed a maximum interest rate but has reserved the right to do so. The amount of interest at this time is fully at the discretion of each individual municipality.

v. DCs are indexed annually based on the Construction Index which has typically resulted in an average annual escalation of approximately 3%. The City's own experience through the completion of a Background Study every 5 years is that the cost of municipal infrastructure tends to increase at higher rates than the Construction Index.

vi. Any interest rate set by the City should consider both the annual cost of inflation/DC rates as well as the impact of locking in of rates that overlap future Background Studies.

ENVIRONMENTAL AND CLIMATE CHANGE MATTERS

11. There are no environmental or climate change matters directly related to the recommendation.

ALTERNATIVES

12. The following alternatives are available for consideration by General Committee:

Alternative #1 General Committee could request security and provide two tiers of interest rates. Tier 1: a lower rate of interest, such as the City's weighted average cost of capital, to developments that provide security. Tier 2: a higher rate of interest, such as the City's weighted average cost of capital plus 5% to developments that do not provide security.

This alternative is not recommended because requesting security may negate the intent of the legislation to incentivize rental housing and institutional development.

Alternative #2 General Committee could eliminate interest requirements for deferred DC payments and for frozen rates.

This alternative is not recommended as the City requires the necessary and timely collection of development charge funds in order to pay for the infrastructure needs of incoming growth. Where development charges are deferred, the City is either required to use its reserves (that could have generated interest revenue) or borrow with associated costs, to fund any shortfall.

Alternative #3 General Committee could set different interest rate(s) than have been proposed in the staff report.

This alternative is not recommended as the interest rates proposed strike a balance between the strategic priorities of promoting affordable housing and development, with the requirement to manage risk and balance the revenues of growth with the cost of growth.

FINANCIAL

13. Based on our review of Bills 108 and 138, the full extent of the financial impacts to the City are unclear. This is, in part, because much of the detail will come in yet to be released provincial regulations.

14. It is essential that the City continue to provide affordable housing options, and limit its financial risk following legislative changes that came into force on January 1, 2020.

LINKAGE TO 2018-2022 STRATEGIC PLAN

15. The recommendations included in this Staff Report support the following goals identified in the 2018-2022 Strategic Plan.

    a) Growing Our Economy

    b) Fostering a Safe & Healthy City

    c) Building Strong neighbourhoods

Appendix A

Table 1 - Summary of Legislative Changes

Topics	Previous Legislation	Bill 108/138	Impacts	In Effect	Risks	Potential Solutions
Payment in Instalments	Municipalities are able to enter into deferred payment agreements if it so chooses. Each municipality determined who qualified for such loans, the requirements for securities, registration of agreements on title and repayment terms including length and interest.	Mandates payment in instalments for non-profit housing over 20 years, for rental housing that is not non-profit and for institutional developments over 5 years. Interest may be charged up to the prescribed rate. The Minister has not prescribed a rate at this time. The Act does not explicitly permit the City to secure these deferred payments from developers.	For Developer: Improves the cash flow position of developers when considering financing these type of developments. For City: Cash receipts will be delayed, impacting the City's cash position. Collection risk. Additional administrative of tracking and collecting over extended periods of time.	January 1, 2020	Collection Risk: There is collection risk relating to mandatory deferred payments. The Act does not explicitly permit the City to secure deferred payments from developers and landowners. The City could potentially face challenges when attempting to collect future payments for developments where ownership changes hands or where owners/developers fail to provide payment when due. Interest Rate Risk: There is a risk that the City does not set an interest rate that is sufficiently high enough to recover the City's cost of waiting for funds.	Collection: In order to ensure that future owners of properties are aware of deferred payment obligations, the City could require that developers enter into an agreement with the City documenting the requirements of the legislation, establishing the payment terms and interest on payments, and requirements to notify future owners. The City could endeavour to have notice of this agreement registered on title to the lands being developed. Where the development is subject to site plan approval, the City could achieve this through language in the site plan agreement. The City could offer a lower interest rate to developers that provide security to the City than the interest rate charged to developers that do not provide such security. Interest Rate Risk: The City could determine its Weighted Average Cost of Capital (WACC) and charge an interest at a sufficient level to recover WACC and limit the amount of risk of future fluctuations.
When DC Amount is Determined	DCs were calculated at the rate in effect at the time of Building Permit issuance when payment is due.	DCs will be calculated on the date of Site Plan application or Zoning By-law Amendment application. Where no application is made, will continue to be calculated at Building Permit issuance. Interest may be charged up to the prescribed rate. The Minister has not prescribed a rate at this time.	For Developer: Provides DC rate predictability for up to 2 years. For City: While the calculation of DCs is much earlier, the payment of DCs is not. The timing change will result in lower DC calculations that do not keep pace with inflation. Additional administration of tracking over extended periods of time.	January 1, 2020	The freezing of rates ignores the rising costs of providing services. If the interest that is charged is not sufficient to recover inflating costs, the result will be a reduced recovery of growth related costs that will need to be funded by other sources.	Set an interest rate that is at least the City's cost of capital as it relates to infrastructure.
Soft Services removed from DCA. Included in Planning Act as Community Benefit Charge.	Growth related capital costs for services such as Parks and Recreation, Libraries, Administration, Parking, etc. are partially recovered through and funded by development charges. DCs are recovered based on the estimated costs of providing the same level of service to a growing community.	These services will now be recovered through and funded by Community Benefit Charges (CBC). CBCs will be recovered based on a % of land value. The Province will be prescribing a maximum rate but has not yet done so. Other legislative requirements offering greater detail are likely to come.	There will no longer be a nexus between growth related costs and recovery. The Province has not yet provided enough information to assess the extent of the impact of this change.	unknown	Risk that a future prescribed maximum % of land value will not be sufficient to recover growth related capital costs at the same level of service that the community has been accustomed to. Potential risk of requiring additional taxpayer funds to recover growth related cost or future reductions in the level of service provided.	Will be revisited once additional details of legislation are released.
Waste Diversion	90% of growth related capital costs relating to waste diversion is recoverable through DCs.	100% of growth related capital costs relating to waste diversion will be recoverable through DCs.	100% of growth related capital costs for this service will now be recoverable.	unknown	None	n/a