**Supports Item No. 4**
**P&E Committee Agenda**
**July 10, 2008**

CITY OF **VANCOUVER**

**ADMINISTRATIVE REPORT**

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| Meeting Date: | July 10, 2008 |

TO: Standing Committee on Planning and Environment

FROM: Director of Planning, in consultation with the Director of Budget Services

SUBJECT: Vancouver (City-wide) Development Cost Levy Inflationary Rate Review

## *RECOMMENDATION*

A. THAT Council approve the adjustment of Vancouver (City-wide) Development Cost Levy (DCL) By-law rates to reflect construction costs and land value inflation from mid-2003 to the end of 2007 as follows:
   i. from $6.00/square foot to $10.20/square foot for residential development at a density greater than 1.2 FSR and for non-residential (e.g. commercial and industrial) development;
   ii. from $1.75/square foot to $3.00/square foot for residential development with an FSR of 1.2 or less; and
   iii. from $2.40/square foot to $4.10/square foot for development in an industrial zone.

B. THAT Council not adjust the Vancouver DCL By-law rates for school use, parking garage, child care use, temporary building and community energy centre.

C. THAT Council approve a grace period of 18 months from the date of Council approval to the date these rate increases come into effect.

D. THAT Council instruct the Director of Legal Services to amend the Vancouver Development Cost Levy By-law to implement the increased DCL rates.

E. THAT Council instruct staff to notify the development industry and affected stakeholders regarding Council approved changes to the Vancouver (City-wide) DCL.

F. THAT Council approve, in-principle, annual inflationary adjustments to all DCL By-law rates (City-wide and Area Specific); and, instruct staff to report back on recommended annual inflationary adjustment and reporting systems, preceded by a report back on resources needed to develop:
- an annual inflation index reflecting change in construction costs and land values;
- an enhanced DCL tracking system and an annual DCL report that meets new Provincial legislative requirements; and
- a public consultation process to engage key stakeholders.

## *CONSIDERATION*

THAT, should Council wish to extend the grace period beyond the 18 months as per RECOMMENDATION C, Council could amend the timing as follows:

G. THAT Council approve a grace period from the date of Council approval to the date these rate increases come into effect of:
i. 18 months for residential rates, and
ii. 24 months for non-residential (e.g., commercial and industrial) rates.

## *CITY MANAGER'S COMMENTS*

The City Manager RECOMMENDS approval of the foregoing and puts forward G for CONSIDERATION.

## *COUNCIL POLICY*

On June 24, 2003 Council approved Financing Growth Policy. The Financing Growth Policy took a comprehensive look at long term, city-wide growth and its associated public facility costs. The Policy sets the framework for how Development Cost Levies (DCLs) are collected and allocated, and it recommends that DCL rates are reviewed every 3 years taking into account inflationary factors affecting construction costs and land values, and other relevant factors.

## *SUMMARY*

Providing amenities and affordability as the city grows are key issues for Vancouver and were highlighted through the EcoDensity public process.

Development Cost Levies (DCLs) are a significant contribution to the City for amenities and affordable housing, and relieve what would otherwise fall to property tax to support. DCLs are a growth-related charge on new construction. DCL revenue is used for growth-related needs in the following categories:

- park land acquisition and improvements,
- replacement (affordable) housing,
- childcare facilities, and
- transportation infrastructure.

The last time that Vancouver (City-wide) DCL rates were reviewed was in 2003. Since then the City has been increasingly falling behind in its ability to provide DCL-funded benefits due to the lack of inflation adjustments to the DCL rates. New facilities face increased costs for land and construction and in the recent period of rapid growth these costs have grown faster than the rate of general inflation in the economy.

To address this issue, the City hired a consultant (Coriolis Consulting Corp.) to develop recommended rates based on combined inflation in land and construction from mid-2003 to the end of 2007.

Based on the analysis, the recommended Vancouver (City-wide) DCL rate increases are:

- $6.00 to $10.20 per square foot for most residential and commercial development;
- $1.75 to $3.00 per square foot for smaller-scale residential - 1.2 FSR or less (e.g., single family, duplex, infill, rowhouse); and
- $2.40 to $4.10 per square foot for development in industrial areas.

The consultant also tested the recommended rates to determine economic impact and found that the recommended rates could be absorbed by the market without affecting housing affordability or significantly deterring development. However, the consultant also noted that some types of redevelopment face viability challenges in the current market.

During the public process that accompanied this work, a key issue identified by industry stakeholders was economic impact, particularly industrial and commercial viability. Two key ways to address viability are:

- <u>Grace period</u>: The grace period is the length of time between Council approval of a new DCL rate and when the rate comes into effect. Typically the City has provided 12 months, and staff recommended 12 months in the initial "Proposal" discussed with stakeholders this spring. However, based on stakeholder concerns and the recognition that land use policy changes (see below) affecting commercial and industrial viability will take time to be felt by the market, staff are recommending 18 months for all uses. Staff are also providing a consideration for 24 months for industrial and commercial rates.

  The difference between a 12 month and 18 month grace period represents approximately $10 million in foregone revenue to the City. Extending this to 24 months (not recommended by staff) would add an estimated $4 million (i.e. total of $14 million) in foregone revenue. Currently, non-residential (e.g., commercial and industrial) uses make up about 33% of City-wide DCL revenues.

- <u>Land use policy changes</u>: In terms of commercial and industrial economic viability, land use policy (e.g., increased density and height, modified land uses) will have a more powerful impact on viability than changes in DCL rates. The Metro Core study is recommending significant density increases as well as separating out competing residential land uses from commercial areas in the downtown. Density increases will also be developed for Central Broadway commercial, and density and land use changes developed for the adjacent industrial areas. Industrial areas in South Vancouver in Marpole and around the new Canada Line transit station are also being reviewed, with a view toward intensifying employment opportunities near the station and adjacent industrial lands.

This report also recommends adopting, in-principle, an annual inflationary adjustment for all DCL By-laws (City-wide and Area Specific). The DCL rate increases in this report apply to the City-Wide DCL area which covers most of the City. However, staff recommend using this approach as a basis for future inflationary reviews of all DCL By-law rates. Annual adjustments would mean smaller, more predictable rate increases in the future, and a more inflation-resilient DCL revenue stream to the City.

The Province recently approved the Local Government "Green Communities" Statute Amendment Act (Bill 27). As a result, the City is required to public an annual report on the collection and use of DCL reserve funds. Stakeholders, both community and industry, also requested better tracking of how DCLs are spent. To achieve this, enhancement to the City's DCL tracking and reporting capabilities will be necessary.

To accomplish the above, this report recommends that staff report back to Council on recommended annual inflationary adjustment and reporting systems for all DCL By-laws. This report back will be preceded by a report on resources needed to develop and consult on these systems.

Inflationary rate adjustments and annual rate updates will help ensure that Vancouver is able to provide an appropriate level of growth-related facilities and services. Enhanced DCL tracking and annual reporting will provide better public access to how DCLs are used to provide public facilities. These facilities are a key element in maintaining the City's livability and sustainability as it grows.

## *PURPOSE*

The purpose of this report is to recommend amendments to the Vancouver (City-wide) DCL By-law rates to reflect inflation in land values and construction costs, and an appropriate grace period before these new rates come into effect. Drawing on the approach used for the City-wide DCL rate, this report also recommends approving, in-principle, annual inflation adjustments to all DCL By-law rates. To implement this annual system, the report recommends that staff report back on the resources needed to develop a recommended annual inflation index. The report back will also include resources needed to deliver enhanced DCL tracking and annual reporting, and associated public process.

## *BACKGROUND*

DCLs are a growth-related charge collected from all new development. They are applied on a per square foot basis and payment is due at Building Permit issuance. Based on the Vancouver Charter, DCL revenues help pay for the following growth-related capital projects:

- park land acquisition and improvements,
- replacement (affordable) housing,
- childcare facilities, and
- transportation infrastructure (e.g., greenways, pedestrian improvements, etc.).

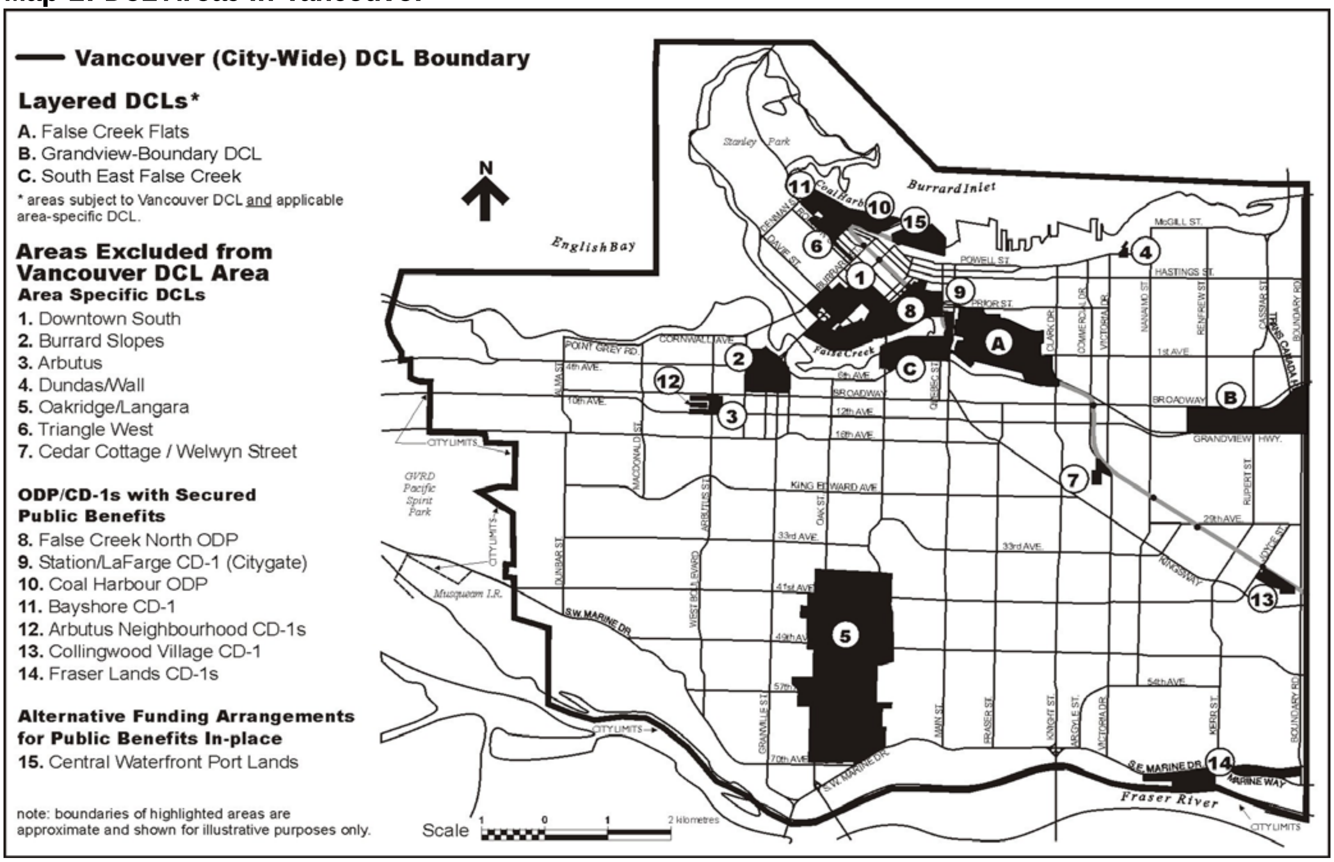
DCLs can also help pay for other engineering infrastructure such as water, sewer and drainage but these projects are not included in the City-wide DCL.

There are eleven DCL areas in Vancouver. Most of the city is covered by the Vancouver (City-wide) DCL. In addition, there are smaller area-specific DCL areas, of two types:

- 7 area-specific DCLs which existed prior to the City-Wide DCL and are not included in it (e.g., Downtown South, Oakridge-Langara); and
- 3 area-specific DCLs which are layered on top of the City-Wide DCL due to particular additional costs for these areas (i.e., Grandview-Boundary, False Creek Flats, Southeast False Creek).

This inflationary review applies to DCL rates in the Vancouver (City-wide) DCL District as shown in Map 1. This is the first inflationary review of City-wide DCL rates since Council approval of these rates in 2003. Rates in the other DCL areas are not under review at this time, however the approach used to adjust the City-wide DCL provides a basis for future inflationary reviews of all DCL By-law rates.

**Map 1: DCL Areas in Vancouver**




## *DISCUSSION*

Vancouver continues to grow and with more people are more demands on City facilities and services. In the face of growth, the City has fallen behind in its ability to provide growth related facilities because DCLs are not keeping up with inflation. New facilities face increased costs for land and construction and in the recent period of rapid growth these costs have grown faster than the rate of general inflation in the economy.

Financing Growth Policy established a number of guiding principles to follow in the establishment and review of DCLs. Some of the key principles guiding this inflationary review of DCL rates are:

- Maintain community livability as the city grows;
- Require new development to contribute to paying for its growth costs and impacts;
- Do not deter development, or harm housing affordability;
- Provide a system that is city-wide and that is consistent and predictable for both the development industry and community;
- Maintain a simple, understandable and transparent DCL system and make rate adjustments based on well-known, readily available and reliable indicators; and
- Consult broadly and develop new rates based on informed input from stakeholder groups.

Staff's "City-wide DCL Inflationary Rate Review: Proposal", circulated to stakeholders in April 2008, contained four key elements:

1. Inflation Adjusted DCL Rates;
2. Analysis of Economic Impacts;
3. 12 Month Grace Period; and
4. Annual System of Inflation Adjusted DCL Rates.

These elements are discussed below.

**1. Inflation Adjusted City-Wide DCL Rates (RECOMMENDATION A)**

The last review of City-wide DCL rates was in 2003. Council approved an increase to DCL rates from $2.50/square foot to $6.00/square foot for residential and commercial (and most other development), and from $1.00/square foot to $2.40/square foot for industrial. These are the current City-wide DCL rates (June 2008).

Staff recommend that Council approve adjusting the Vancouver DCL By-law rates to reflect construction costs and land value inflation from 2003 to 2007. The proposed DCL rates are based on a review of inflationary trends and indicators conducted by Coriolis Consulting Corp. (see Appendix A for a Summary - copies of the complete report are on file with the City Clerk and on the project website www.vancouver.ca/financegrowth ).

The consultant concluded that because the City uses DCL revenues to pay for land acquisition and construction costs for new parks and park improvements, replacement (affordable) housing, childcare, and transportation infrastructure, the DCL rate increase should be based on a blend of land and construction cost inflation. Staff estimate the ratio City expenditures for DCL capital projects is approximately 65% related to land acquisition and 35% related to construction costs.

The consultant reviewed several potential inflationary indicators and recommended that construction cost inflation be determined using the Statistics Canada Non-Residential Construction Price Index (NRCPI) for Vancouver. Land value inflation does not have a similar, readily available indicator and it was measured based on a review of changes in assessed land value using BC Assessment Authority (BCAA) information. Recommended DCL rates are based on the annual change in construction costs and land values, compounded from mid-2003 to the end of 2007 as shown in Table 1.

**Table 1: Current and Recommended City-wide DCL Rates**

| Type of Development | Current DCL Rates Established in 2003 (per sq. ft.) | Recommended 2008 DCL Rates (per sq. ft.) |
|---|---|---|
| Residential (>1.2 FSR), Commercial & Other Uses | $6.00 | $10.20 |
| Residential (up to 1.2 FSR) e.g. single family, duplexes, and rowhouses | $1.75 | $3.00 |
| Industrial Zones | $2.40 | $4.10 |

The City-wide DCL By-law includes a number of uses that have lower DCL rates such as daycare, and elementary and secondary schools. RECOMMENDATION B recommends that the rates for these uses not be adjusted to reflect inflation as their lower rates reflect their lower growth costs and in many cases, the rate is intentionally nominal.

## 2. Economic Impact

The City asked the consultant to recommend new DCL inflation-adjusted rates that could be introduced without causing significant negative impacts on the viability or rate of new development, or harm affordability. Economic impact testing was conducted when City-wide DCL rates were first established in 2003 and a similar approach was used in this review.

For this review the consultant conducted case studies of typical redevelopment projects, including residential, commercial and industrial sites, to identify potential impacts of the increased DCL rate. The consultant concluded that the proposed DCL rates will not materially affect the overall pool of redevelopment sites available, and will not negatively impact the affordability of new residential units or commercial/industrial space.

The consultant report also identified that some non-residential redevelopments face challenging market viability under current market conditions. Key examples include redevelopment of office projects Downtown or along Central Broadway, and industrial projects in I-2 and I-3 zones. Sensitivity analysis conducted by the consultant showed that relatively small changes in various factors (e.g. changes to interest rates, revenues, or construction costs) can have a significant impact on development viability. The consultant also noted that increases in allowable density can also have a significant impact.

Feedback from development industry stakeholders expressed concerns that increased rates could have a dampening effect, especially on commercial and industrial redevelopment (see Appendix B – Stakeholder Feedback).

Economic viability of commercial and industrial development is very important to the City. Based on the consultant analysis and discussions with the development industry, staff believe that upcoming land use policy changes will have a much more profound impact on redevelopment viability than the increase in City-wide DCL rates. Several major policy initiatives which relate directly to improving economic viability include:

- Metro Core Jobs and Economy Land Use Plan: proposals for the Downtown (scheduled for Council in September 2008) contain recommendations to increase permitted commercial density and building heights, and future work will similarly address Central Broadway and adjacent industrial areas, as well as the eastern Core:
- Marpole Industrial and Station Area Planning: a land use planning program has just launched for the Cambie/Marine Canada Line station and the nearby industrial area, which includes I-2 zoning, with a view to intensifying employment opportunities near rapid transit; and
- False Creek Flats: a new land use and transportation plan will be developed for this area which includes I-2 and I-3 zoning.

Beyond these land use initiatives, Council has also approved a property tax shift having the effect of lowering the share of taxes paid by the non-residential sector.

The consultant and staff also assessed the competitiveness of Vancouver's DCL rates. The consultant noted that direct comparison is not particularly relevant as rates in other municipalities reflect different growth costs (and projects). DCL rate categories also vary considerably between municipalities. However, the key findings are:

- Vancouver's recommended new residential rates would be near the highest in the region and would be slightly below rates in Richmond and Surrey;
- Vancouver's commercial rate would continue to be the highest in the region, slightly above Richmond and Surrey; and
- Vancouver's industrial rate would be lower than Richmond and similar to Coquitlam and Surrey.

### 3. Grace Period (RECOMMENDATION C)

The grace period was seen by stakeholders as a way to help address concerns about economic viability. Staff's initial proposal was for a 12 month grace period. Based on feedback from the development industry, and recognition that upcoming land use policy changes affecting commercial and industrial viability will take some time to be felt by the market, staff recommend an 18 month grace period for residential and non-residential (e.g., commercial and industrial) rates (RECOMMENDATION C).

The grace period is the time between Council approval of new DCL rates and the date when the new rates come into effect. Typically, staff recommend a one year grace period to implement new DCL rates as this timing allows developments, in-process, to reach building permit issuance before new DCL rates taking effect. Staff have reviewed current development permit processing times and note that the time from receipt of a development permit application to issuance of a building permit is averaging nine months to one year. Staff note that for some projects, especially larger, more complex projects this timing can extend beyond one year into the pre-application process. The 18 month grace period will give more time to projects now in-process to reach building permit issuance.

Though not recommended by staff, a consideration has been provided to Council that extends the grace period from 18 months to 24 months for non-residential rates as a further response to feedback from the development industry (CONSIDERATION G). Extending the grace period will result in additional foregone revenue, estimated at $4 million.

**4. System of Annual Inflationary Adjustments and Annual Reporting for All DCL By-laws (RECOMMENDATION F)**

Inflationary rate adjustments and annual rate updates will help ensure that Vancouver is able to provide an appropriate level of growth-related facilities and services. These facilities are a key element in maintaining the City's livability and sustainability as it grows. Recommended DCL rates account for changes in construction costs and land values between mid-2003 and December 2007 (RECOMMENDATION A). Staff also recommend, in-principle, annual inflationary adjustments that could be applied to all DCL By-law (City-wide and Area Specific) rates to help keep pace with future inflation (RECOMMENDATION F).

Historically, both land and construction costs have increased and decreased, although the overall trend has been upward. Annually adjusted rates would allow for smaller changes in DCL rates year to year. This would avoid large changes over longer periods of time and allow for greater predictability for the development industry. Importantly, it would also provide inflation-adjusted DCL revenue to pay for public facilities required due to growth.

Annual inflationary rate increases are recommended by the Provincial Development Cost Charges Best Practices Guide and similar approaches are used by many different public authorities. For example, the City already adjusts its building and development fees on an annual basis to reflect inflation. The consultant report notes that annual adjustment requires a well-known, readily available, reliable set of indicators.

Development industry feedback notes a concern that construction costs and land values are volatile. Because of this volatility, annual inflation adjusted rates could be highly variable. Staff share this concern and will consider the use of three, or possibly five, year averaging of annual inflation rates to moderate annual rate variations. This is similar to the approach used by the City regarding property tax rates.

Tracking and reporting DCLs are another important element of the DCL system. Recently, the Province approved Bill 27 (Local Government "Green Communities" Statute Amendment Act) which amends the Vancouver Charter and requires the City to publish an annual report on the use of DCL reserve funds. Feedback from development and community stakeholders expressed a strong desire to see more information about how much DCL revenue has been collected and how DCLs have been spent. A summary of City-wide DCL revenue, spending, and capital project examples is provided in Appendix C.

RECOMMENDATION F asks Council to approve, in-principle, annual inflation adjustments to all DCL By-law (City-wide and Area Specific) rates. To implement this annual system, the report recommends that staff report back on the resources needed to develop a recommended annual inflation index, and enhanced DCL tracking and annual reporting systems. Specifically, additional resources are needed for:

- Development of an annual, blended construction cost and land value inflation index;

- Enhancement of the DCL tracking system and reporting system to meet Bill 27 legislative requirements by mid-2009; and

- Public consultation, stakeholder engagement, and communication of changes to the DCL system.

## *PUBLIC PROCESS*

The City-wide DCL inflationary rate review was initiated in early 2007. A Newsletter describing the purpose of the review was shared with industry groups, posters were placed in the Inquiry Centre, and a web site was established in mid-2007. Industry groups assisted this process by circulating the City's Newsletter with their own mail-outs or e-newsletters.

On April 21, 2008 a "Proposal" to adjust the City-wide DCL rates for inflation was circulated to stakeholders, posted on the web site, and made available in the Inquiry Centre. The "Proposal" described the key potential changes to DCL rates due to inflation. The consultant report of inflationary factors and market impacts was also was circulated in early 2008 to industry stakeholders and posted on the web. Ads providing details of the proposed rates were placed in the Courier and major ethnic newspapers in May 2008.

On May 9, 2008 a stakeholder meeting was held to discuss the "Proposal" with approximately 20 representatives of both the development industry and community organizations that use and/or operate DCL-funded facilities attending. Written responses to the "Proposal" were requested by June 6, 2008. Staff also met separately with representatives of the National Association of Industrial and Office Properties (NAIOP), Greater Vancouver Home Builders Association (GVHVA), and the Urban Development Institute (UDI). Appendix B contains all written submissions received.

Generally, stakeholders agreed on the value of having new development contribute toward community facilities and the overall livability of the city. Community representatives stressed the need to deliver community facilities in-step with new development, and they expressed concern about the City falling behind in its ability to provide the facilities. Staff note that one of the key issues identified during the EcoDensity process was the need for new amenities to support growth. Community and development industry representatives both strongly supported better reporting of DCL collections and spending.

Most stakeholders also generally supported the need for regular adjustment of DCL rates to address inflation. The Urban Development Institute (UDI) supports regular, more predictable changes to DCL rates. The National Association of Industrial and Office Properties (NAIOP) do not support any DCL increases (they suggest a waiver) or annual rate adjustments. Both UDI and NAIOP expressed concerns about the amount of the overall increase and the proposed 12 month grace period for implementing the new rates, especially in the face of challenging market conditions for office and industrial development.

## *FINANCIAL IMPLICATIONS*

DCL revenue joins with property taxes to help pay for growth related capital costs. As a financial tool, DCLs are a significant revenue source for the Capital Plan. Since inception in 2000, City-wide DCL revenue is approximately $90 Million and as of April 2008 approximately $74 Million is spent or committed to growth-related facilities across the city. This does not include City-wide DCL revenues collected and targeted for spending in South East False Creek (see Appendix C for details).

At the current DCL rates, DCL revenue is estimated to recover 80% of the City-wide growth costs for DCL projects. However, since the current City-wide DCL rates were set in mid-2003, inflation in construction costs and land values has been averaging about 14% per year. This annual inflation results in the City falling behind in its ability to provide growth facilities.

RECOMMENDATION A adjusts DCL rates to reflect inflationary change from mid-2003 to the end of 2007. Had City-wide DCL rates been adjusted annually to reflect inflation between 2003 and 2007, staff estimate approximately $20 million in additional DCL revenue would have been collected.

A key part of DCL revenues is the role they play in the Capital Plan. Table 1 illustrates past and projected DCL revenues and their contribution toward the Capital Plan.

**Table 1: DCLs and Capital Plan**

| | **Total Projected Revenue (3 years)** | **Average Projected Annual Revenue** |
|---|---|---|
| **2006-2008 Capital Plan**<br>Actual & Projected DCL Revenue* | $50 million | $17 million |
| **2009 - 2011 Capital Plan**<br>Projected DCL Revenue: Recommendations A & C | $82 million | $27 million |

* Not including SEFC City-wide DCL revenue.

Of total DCL revenue generated, residential development contributes about 66% and non-residential (e.g. office, retail, industrial) contributes about 33%. The projection for the 2009-2011 Capital Plan assumes slightly less development than in the previous 3 year period, and the higher revenue is due to the amount of the recommended DCL rate increase and projected annual inflationary adjustments.

RECOMMENDATION C goes beyond the typical 12 month grace period by providing an 18 month grace period for all uses. CONSIDERATION H would provide a 18 months for residential and 24 months for non-residential development. The financial implications for DCL revenue of providing a longer than 12 month grace period are shown in Table 2.

**Table 2: City-wide DCL Grace Period - Financial Implications for 2009-2011 Capital Plan**

| Grace Period | Total Projected Revenue (3 years) | Average Projected Annual Revenue | Foregone DCL Revenue - Difference From 12 Month Grace Period |
|---|---|---|---|
| 12 Month Grace – All Uses | $92 million | $31 million | N/A |
| **RECOMMENDATION C**<br>18 Month Grace - All Uses | $82 million | $27 million | **-$10 million** |
| **CONSIDERATION H**<br>18 Month Grace – Residential<br>24 Month Grace - Non-Residential | $78 million | $26 million | **-$14 million** |

Staff note that inflationary adjustments will catch-up DCL rates to better reflect the true costs of providing new growth facilities. However, there is no catch-up for foregone DCL revenues. New inflation adjusted rates only recover growth costs going forward. This is a key reason to keep rates adjusted annually.

## *SOCIAL AND ENVIRONMENTAL IMPLICATIONS*

DCLs provide an important part of the social infrastructure of the City by contributing to the funding of growth-related capital projects. This includes: new park land acquisition and park improvements; acquisition of sites and construction of child care facilities; and, acquisition of sites and/or renovation of non-market housing sites and buildings

In addition to contributing to social infrastructure, DCLs also contribute toward environmental sustainability. DCLs support provision of smaller, more affordable and compact housing which has a smaller ecological footprint by basing the charge on the number of square feet rather than on a per unit basis. The DCL also encourages re-use and adaptation of existing buildings by exempting renovations and heritage restoration from DCL charges. Transportation improvements provided by DCLs focus on pedestrian, bicycle, and transit throughout the city also contribute toward a reduced carbon footprint.

## *CONCLUSION*

Vancouver will continue to grow and with more people are more demands on City facilities and services. In the face of growth, the City has fallen behind in its ability to provide growth related facilities because City-wide DCLs are not keeping up with inflation. New facilities face increased costs for land and construction and in the recent period of rapid growth these costs have grown faster than the rate of general inflation in the economy.

This report recommends amendments to the Vancouver (City-wide) DCL By-law rates to reflect inflation in land values and construction costs, and an appropriate grace period before these new rates come into effect. Drawing on the approach used for the City-wide DCL rate, this report also recommends approving, in-principle, annual inflation adjustments to all DCL By-law rates. To implement this annual system, the report recommends that staff report back on the resources needed to develop a recommended annual inflation index. The report back will also include resources needed to deliver enhanced DCL tracking and annual reporting, and associated public process.

Inflationary rate adjustments and annual rate updates will help ensure that Vancouver is able to provide an appropriate level of growth-related facilities and services. Enhanced DCL tracking and annual reporting will provide better public access to how DCLs are used to provide public facilities. These facilities are a key element in maintaining the City's livability and sustainability as it grows.

* * * * *

**"INFLATIONARY ADJUSTMENTS TO DCL RATES",** Coriolis Consulting Corp., December 2007

The text below is an excerpt of the Summary from the complete report. Copies of the full report are on file with the City Clerk.

**Summary**

In 2003, the City of Vancouver adopted a policy of reviewing its Development Cost Levy (DCL) rates every three years or as directed by Council. The City has decided that it is timely to consider adjusting existing rates:

- The City-wide DCL rate. The current rate is $6.00 per sq.ft. for residential and commercial space and $2.40 per sq.ft. for industrial space. These rates were approved by Council in June 2003 and have not been adjusted since then.

- The low density residential City-wide DCL rate. The current rate for residential projects built at densities of 1.2 FSR or less is $1.75 per sq.ft. This rate was approved by Council in July 2006 and has not been adjusted since then.

There has been substantial inflation in land values and construction costs since these DCL rates were set. The City is considering adjusting these DCL rates to reflect inflation in the City's costs (construction and land acquisition) to create the amenities and infrastructure funded by these DCLs. The City retained Coriolis Consulting Corp. to recommend new DCL rates based on inflationary indicators that could be introduced without causing any significant negative impacts on the viability or rate of new development in the area.

The City also asked us to suggest a method to update the DCL rates more frequently to reflect changes in the capital cost of providing new amenities and infrastructure. Therefore, we also examined possible approaches that could be used to adjust DCL rates annually in the time period between detailed reviews.

**Approach**

Our approach to this analysis was to examine the expected financial performance of a variety of hypothetical redevelopment projects in the City at the current DCL rate and then compare this with the expected performance of the same project at an increased DCL rate to identify any impacts. Our evaluation focuses on determining whether or not an increased DCL will reduce the number of sites that are financially attractive for redevelopment. If it does, then the supply of development sites will be reduced which could impact the pace of development and market prices.

With input from City Staff, we identified 12 hypothetical development project case studies to evaluate. These case studies are intended to be broadly representative of the range of typical redevelopment projects that are currently occurring (or anticipated to occur under existing land use policies) in the parts of the City that are subject to the City wide DCL. While it is not possible to analyze the impact of a change in DCLs on every project in the City, these case studies represent a wide range of potential redevelopment projects in each of the DCL policy areas in terms of land use, density, building form, and location. Therefore, any impact on these hypothetical projects from an increased DCL will be broadly indicative of the potential impact on many redevelopment projects in these policy areas.

**Recommended DCL Adjustments**
The City uses DCL revenues to pay for land acquisition costs and construction costs for new transportation infrastructure, sewer, water, drainage, parks, child care, and replacement affordable housing. Therefore, a DCL adjustment should be based on inflation on land values and construction costs, rather than general inflation in the overall economy (e.g., CPI). In recent years land values and construction costs have been increasing at rates significantly higher than general inflation in the economy. Our analysis of different inflation indicators indicates that a range of DCL rates could be appropriate depending on which inflation indicator is used (inflation on construction or inflation on land). Inflation in land value has (over the relevant time period) been higher than inflation in construction costs. Because the City's future expenditures involve land acquisition and construction, a blend of the two inflation rates could be used. In order to provide the City some flexibility in setting the adjusted rate, we analyzed the total impact of adjusting DCLs at the higher rate, on the premise that if there are not significant impacts at this maximum rate there would not be impacts at a lower, blended rate.

1. The City-wide DCL rate for residential and commercial space ($6.00) would increase to $8.86 if the adjustment is based solely on construction cost inflation. The rate would be $11.44 if based solely on land value inflation.

2. The low density residential DCL rate ($1.75) would increase to $2.66 if the adjustment is based solely on construction cost inflation. The rate would increase to $3.43 if the adjustment is based solely on land value inflation. At the higher rate there would be no significant impacts on the financial viability of new development or on the pace of new development in this category. If a blended inflation adjustment is used, the rate would be between $2.66 and $3.43. Any rate in this range will not have a significant impact.

3. The City-wide DCL rate for industrial space would be between $3.54 and $4.58.

Revised City-wide rates (even at the high end of these ranges) would have no significant impact for most kinds of development in most parts of the City. There are some areas where there might be impacts:

- Some office development sites in the DD-C district would be negatively affected. However, sensitivity analysis showed that a relatively small increase in density or in market rents would provide enough additional value to offset the impact of the higher DCL.

- Some C-2 sites on the east side of the City will be negatively affected, particularly those with existing development with FSR of 0.6 or more. This impact is confined to a portion of the C-2 sites in a few areas including Kingsway, East Hastings, Commercial, Fraser, and Victoria Drive. However, many properties have existing FSR below 0.6, so the total supply of development properties should not be noticeably reduced. The impact could be offset by allowing density increases. Sites with existing FSR of 0.5 or less will continue to be redevelopment candidates at the higher DCL rate and sensitivity analysis shows that a relatively small increase in density or in project revenues provides enough value to offset the impact of a higher DCL rate.

- There are some categories of redevelopment that are not viable now and that will be even less viable at the new rate. This group mainly includes properties designated for low density industrial and office that have good quality, revenue-generating improvements. The higher rate will postpone redevelopment of these sites even further into the future, even though their current development density is low. However, some redevelopment will still occur in these locations in cases where the land is vacant, the existing improvements are functionally obsolete, commercial rents for new space are high, or developers acquired sites before recent escalation in land value.

**Recommended Approach to Annual Adjustments**

In our view, a system of automatic inflation adjustments is a good idea in principle for two reasons: first, it results over time in a gradual adjustment of the DCL rate rather than large jumps at long intervals; second it produces an inflation-adjusted revenue stream for the City. The basic elements of the system should be:

1. An annual adjustment based on a well-known, readily available, reliable indicator.

2. Major reviews at fixed time intervals, say every 3 to 5 years.

An annual adjustment requires a well-known, reliable, appropriate index. If the City’s costs were primarily driven by construction, it would make sense to use an index such as Statistics Canada’s non-residential construction cost index and then adjust for accumulated land value escalation in the periodic major review. However, we understand that over half of the City’s expected cost is land acquisition, so during periods of rapid inflation in land value the City would have declining purchasing power if it only adjusted DCL rates based on construction cost inflation.

There is not a readily available indicator of land value inflation. The assessment base (land only) could be used as the basis for such an indicator, if a reliable, simple approach can be developed to “net out” land value increases due to non-inflationary factors (e.g. rezoning). Even if a Vancouver-specific land value index can be created, it will be necessary to develop a mechanism to deal with volatility. Construction cost inflation has varied considerably over the last two decades, but the inflation rate has always been above zero. Land values, on the other hand, have declined over some time periods (see Exhibit 2A). Linking DCL rates precisely to the change in land values might result in reducing the DCL rate at some adjustment dates.

In our view, the City has these options:

- Adjust for construction cost inflation at the yearly update and adjust for accumulated land value changes at major periodic reviews.

- Create a Vancouver-specific land value inflation index and use this to make annual DCL adjustments based on a blend of construction cost inflation and land value escalation. The blended rate might incorporate a conservative approach to land value change, to avoid a highly volatile DCL pattern over time.

- Adopt a different strategy for land acquisition. If the City put a priority on acquiring land early, it could eliminate the need to adjust the DCL to reflect changing land values. If the City borrowed the funds to acquire land and applied interest charges in the DCL rate, the resulting DCL rate would probably be lower over the long term than a rate that must be adjusted upward to reflect land value growth (which is likely to be higher than interest rates over the next decade or so).

Developing a land value index will take a significant amount of research and analysis, particularly if there is desire to avoid a volatile DCL. In the short term, we recommend:

- Adjusting the DCL to reflect actual construction cost and land value inflation to 2008, using a blended rate that matches the City's mix of construction and land acquisition costs.

- Over the next one or two years, adjust the DCL annually based on construction cost inflation and a conservative estimate of land value escalation based on a sample of projects.

- During this time, develop a detailed approach for dealing with the land component, which might be a land value index or a different approach to land acquisition.

- Update the DCLs and introduce a new inflation adjustment mechanism in one or two years.

In order to give the development industry reasonable notice of annual adjustments, we recommend that the date of publication of the new rate and the date the new rate comes into force be different. For example, the City could publish on September 30 the new rate (based on the previous year's construction cost inflation) that will come into force on January 1. This means the rate will lag construction cost inflation by a three month period, but we think it is reasonable to provide lead time regarding the new rate.

## STAKEHOLDER FEEDBACK TO THE CITY-WIDE DCL INFLATIONARY RATE REVIEW

### Letter #1 - Urban Development Institute

**URBAN DEVELOPMENT INSTITUTE – PACIFIC REGION**
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Vancouver BC V6B 1P2 Canada
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June 6, 2008

Randy Pecarski
Senior Planner, City Plans
Community Services
City of Vancouver
453 West 12th Avenue
Vancouver, BC V5Y 1V4

Dear Mr. Pecarski:

***Re: Proposed City-wide Development Cost Levies (DCLs)***

I would like to thank you for inviting Urban Development Institute (UDI) representatives to the May 9, 2008 stakeholder meeting on the City's proposed changes to its Development Cost Levies (DCLs), and for speaking to our Liaison Committee about the issue on May 21, 2008. We agree with you that a special meeting with UDI on this matter is needed, and we are arranging one for mid-June. However, before the meeting we would like to summarize in writing some of the initial comments UDI members have raised at previous meetings about the City's proposals and the December 2007 Coriolis report, *Inflationary Adjustments to DCL Rates*.

We would like to reiterate that UDI and the industry understand and support the concept of Development Cost Levies. In order for development to occur, infrastructure is needed and must be funded. We do however have some questions and concerns with what is being proposed at this time. These are important questions given the substantial increases in rates, which are equivalent to a 14% increase every year since the city-wide DCLs have been collected.

#### What has been funded thus far with the City-wide DCLs?

The Financing Growth Policy was approved in 2003. For several years now, the City has been collecting a significant amount of DCLs from the industry, businesses and new homebuyers. What projects have been funded by the DCLs, and what projects will be funded in the future? This information would not only assist us in our comments, but is also important for the residents in neighbourhoods where development is occurring. The City should be more proactive in providing this information to stakeholders on an ongoing basis. It is also important that this information be made available before Council moves to increase DCL rates.

**What are the City's true costs of DCL projects?**

This is directly related to the previous issue. The Coriolis report estimates what the City's costs are based on how much land values and construction costs have increased over the past few years. While this information is useful, it does have limitations. The consultant notes the difficulty in assessing which inflationary factors to use in the analysis. In fact, more work is required to determine inflationary increases on ongoing basis. In addition to this, different types of projects (e.g. roads, housing and parks) are going to be impacted differently by increases in land prices and construction costs. In other communities, when Development Cost Charges (DCCs) are calculated to reflect inflation, UDI is usually provided with the actual costs of recent municipal projects. Staff outlined what they thought projects were going to cost to build, and then the actual costs. To have a better understanding of the cost pressures facing the City, UDI would like to receive this type of information.

**Replacement Affordable Housing DCLs**

It is noted in the Coriolis report that "The City can use DCL revenues to pay for transportation infrastructure, sewer, water, drainage, parks, child care, and replacement affordable housing (to replace any low income units lost in the redevelopment process)." We believe the housing costs are significantly lower since Council passed the "Rate of Change" regulations a year ago, which establishes, in effect, a moratorium on the redevelopment of rental buildings. This policy will be in place until at least later in 2009, when a City review of the rental housing market is expected to be completed. If our members are being restricted from redeveloping these sites, how much replacement affordable housing is required? This is an important matter as replacement housing represent 32% of the DCLs. DCLs are supposed to pay for the costs of growth. The City may now be collecting money from development that is unrelated to growth. We suggest the City review the recent Supreme Court of Canada case *Kingstreet Investments vs. New Brunswick*.

**Impact on Development**

As noted above, the proposed increases are very substantial. We believe that they will have a significant impact on development – especially commercial and industrial development that the City is seeking through initiatives such as the Metro Core Jobs and Economy Land Use Plan. Exhibit 9 (Impact of Increased DCL on Land Value and Development Opportunity) on page 28 of the Coriolis report exemplifies this. Under the last column (Is development financially attractive under target DCL?), only two types of development are deemed to be viable and five are not. Some sensitivity analysis is done on the scenarios, but in several cases it is determined that redevelopment could remain unviable. This includes some scenarios in which a lower DCL charge, than what is being proposed, is applied. In addition, where development is deemed to be viable, the land value under redevelopment is not much higher than it is under existing use, and a 15% profit is almost not met. This is important because given the recent changes in financing as a result of the sub-prime issue in the United States, a 15% profit may not be viewed by lending institutions as enough to properly manage risk. This is especially true for smaller development companies who may not be able to participate in the market. We believe redevelopment may also be delayed because expectations by landowners will not be met, and they will be reluctant to sell their parcels. These issues need to be considered because redevelopment could be restricted by the increases.

As we noted in our response to the rate changes for the Downtown DCLs, "It also cannot be forgotten that the DCLs are only one cost pressure generated by the City. There are others.

Other fees have and will likely continue to increase, and if sites are rezoned, there will be further charges. Regulatory costs continue to climb. There will likely be new regulations and costs associated with the City's Green Building Strategy that is forthcoming next year. These cumulative costs, coupled with rising land and construction costs, are making Vancouver the most expensive place to live and work in Canada, which is undermining our competitiveness." These points are still valid today.

**Grandfathering / Grace Period**

One way to lessen the impact of the increases on in-stream development projects is to either grandfather applications that are currently in process, or extend the grace period. Staff are recommending a 12 month grace period. We do not believe this is enough. It should be 18 months (if not 24 months), which UDI recommended for the Downtown South DCL increase, and Council adopted. Our reasons are the same. Rezonings and Development Permits are taking longer to obtain. At our Liaison Committee meetings with City staff (including the May 21st one which you attended), UDI members have been constantly reminded that because of the Olympics, other priority projects, and substantial changes in staffing, the development review process will be significantly delayed for the next few years. Another option that should be explored was raised at the May 9th meeting. The City could step up the rates over time, so there is less of an impact.

**Increasing densities**

We are pleased City staff requested that Coriolis review the impact of this option on the viability of projects. We believe it should be considered. In combination with other strategies, this approach could make some projects more feasible. It also supports other City policy initiatives, such as EcoDensity and the Metro Core Jobs and Economy Land Use Plan.

**Annual Inflationary Increases**

One of the issues that the City has asked UDI to address is the need for annual inflationary increases. UDI has for a long time supported annual updates to fees and charges, so there are no significant and surprise rate increases. This is still our position. In terms of how to calculate the increases, UDI is willing to meet with staff to discuss the various options outlined in the report. We do, however, reiterate that there is a need incorporate the City's actual project costs in this analysis.

Once again, thank you for meeting with UDI, and we look forward to our next meeting in mid-June. I hope our comments will assist you in your ongoing analysis, and I look forward to working with you on this and other initiatives.

Yours truly,

Jeff Fisher
Deputy Executive Director

## Letter # 2: National Association of Industrial and Office Properties

naiop
National Association of Industrial and Office Properties
*The Forum for Commercial Real Estate*

City of Vancouver
453 West 12th Avenue
Vancouver, B.C.
V5Y 1V4

Attention: Mr. Randy Pecarski, MCIP
Senior Planner, City-Wide & Regional Planning

**RE: CITY-WIDE DEVELOPMENT COST LEVY - INFLATIONARY RATE REVIEW**
**NAIOP COMMENTS**

Dear Mr. Pecarski:

Thank you for your inviting us to your stakeholder meeting on May 9th and speaking to our group on May 23rd, in regards to the proposed City-Wide Development Costs Levy ("DCL") increases. The Vancouver chapter of the National Association of Office and Industrial Properties ("NAIOP") represents the major landlords, developers, and other participants of commercial and industrial real estate in Vancouver and is especially well suited to comment on this issue.

Given the number of challenges of undertaking any commercial or industrial development in the City of Vancouver, any increase the DCLs will have a negative impact and further limit the scarcity of City's business oriented real estate. The proposed increases amount to a 70% increase over the existing DCL rates.

We ask that the City consider the following comments:

**"Inflationary Adjustments to DCL Rates" Coriolis Consulting Corp December 2007**

It is our opinion that this report, prepared for the City of Vancouver, is inaccurate as a number of the development assumptions used in the financial models are not realistic. We believe a number of costs are understated and as a result, what is shown as feasible projects are not achievable.

**"Metropolitan Core Jobs and Economy Land Use Plan"**

As identified in the Metropolitan Core Jobs and Economy Land Use Plan, having a healthy supply of commercial and industrial real estate is vital for future job growth and economic activity in the City. The increasing of the DCLs is counter to this objective. By adding additional hurdles, the City will negatively impact the amount of new development.

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**City of Vancouver Competitiveness**

There is currently a significant amount of office and industrial development occurring in municipalities outside of the City of Vancouver. For the City of Vancouver to remain a place for businesses to locate, and for providers of employment based real estate to continue to provide homes for these businesses, the City should find ways of encouraging new development. There are numerous challenges commercial developers face when attempting to develop new facilities in Vancouver, increasing the DCLs adds to the number of obstacles and is sending the wrong message. Developers, along with major tenants, will look to the other municipalities to meet their growth objectives.

**Encouraging of New Development**

In light of the need for more jobs related real estate to support the economic growth of the Vancouver, the City should focus its efforts to encourage new developments and provide an incentive based program. The City should consider waiving Development Cost Levies and Community Amenity Contributions. In addition, efforts should be made to shorten the approval and permitting process.

**Phasing-In of Increase/Grace Period**

The increase proposed is very substantial and should be phased over a number of years as opposed to one lump sum increase. Furthermore, the grace period should be as long as possible as it will take a significant length of time for some major projects to makes their way through the City of Vancouver approval process. These projects have been planned based on the exiting DCLs, and to make an increase mid-stream would further hamper the viability of these projects.

Any increases in the Development Cost Levies by the City of Vancouver will further limit the economic growth of the City. It is not supported by the commercial and industrial development community and NAIOP. We believe the City should play a better role in the encouragement of new development.

Thank you for the opportunity to provide our comments and we would be happy to discuss this issue further. We look forward to continuing the working relationship between the City of Vancouver Planning Department and NAIOP Vancouver..

Yours truly,

**NATIONAL ASSOCIATION OF OFFICE AND INDUSTRIAL PROPERTIES**

Geoff Heu
Development Issues Chair – NAIOP Vancouver
Dir: (604) 713-6464

## Letter #3: Better Environmentally Sound Transportation

Better Environmentally Sound Transportation (BEST)

Correspondence received via e-mail, June 4, 2008.

Randy,

Per your questions on the issues annunciated in your letter of May 26, 2008

1.Inflationary Adjustments – Yes we support adjustments for inflation
2. Proposed Inflation-adjustment Rates – The proposed rates and amounts seem reasonable, and not unfair to the development community. As one participant noted, even after the increases, the levies will amount to less than 3% of the construction costs per square foot.
3. The proposed grace period is an equitable way to deal with the issue. It both ensures that the industry begins to pay a rate that accounts for inflation in the past 5 years and gives the industry time to adjust.
4. Yes there should be annual adjustments. And yes, the formula should include the potential for values to drop, although they will not.

Thanks for including us on the list of stakeholders.

Marg

Margaret Mahan
Executive Director
BEST
604.669.2860

## CITY-WIDE DCL SUMMARY: REVENUES AND SPENDING

Below is a table summarizing revenues collected, and spent and/or committed (to be spent) based on Finance Department's records as of April, 2008. The totals exclude DCLs collected for South East False Creek. This is an un-audited statement and all figures should be considered as draft, representative numbers only.

| City-Wide DCL | | | |
|---|---|---|---|
| **DCL Capital Projects** | **Total (April 08)** | **Spent & Committed** | **Remaining Balance** |
| Replacement Housing | $ 29,000,000 | $ 19,800,000 | $ 9,200,000 |
| Daycare | $ 5,600,000 | $ 6,400,000 | $ (800,000) |
| Park | $ 39,300,000 | $ 36,200,000 | $ 3,100,000 |
| Transportation | $ 16,000,000 | $ 11,800,000 | $ 4,200,000 |
| **Totals** | **$ 89,900,000** | **$ 74,200,000** | **$ 15,700,000** |

The following is a summary of significant projects funded in part by DCLs.

**Replacement Housing:**
DCLs collected have been used to acquire sites and buildings and to provide capital grants for the construction and renovation of housing, including:
- Several SRO hotels to be operated by non-profit housing providers, including the Stanley/New Fountain Hotel and the Pennsylvania Hotel.
- Several sites, including 337 West Pender and three of the 12 sites now being developed as part of the City/Provincial partnership (16th and Dunbar, 7th and Fir, Broadway and Fraser).
- A contribution to the Doug Storey Residence, which directly replaces the Passlin Hotel as part of Millennium's L'Hermitage development.
- The City contribution towards 200 non-market units at Woodward's.

**Child Care**
A variety of Childcare projects have been funded including:
- Champlain Heights Daycare
- #1 Kingsway Childcare Centre
- Learning Tree Day Care and Playhouse Child Development Centre
- Redevelopment of Little Mountain Neighbourhood House
- Woodward's Childcare Centre

**Parks**
Parks projects include land acquisition, park development and park upgrading. Example projects include:
- New Park Land Acquisition & Development– various sites
- Sports Fields - Synthetic Turf – Trillium (2 fields), Vancouver Technical Secondary and Point Grey/Kerrisdale Park
- Playgrounds – Replacements & Upgrades – various sites
- Neighbourhood Park Renewal e.g. Oppenheimer, Sunset, Tecumseh
- Woodward's Park Development

**Transportation**
Transportation projects focus on a range of transportation-related improvements, including:
- Downtown Transportation Plan imlementation - 2 way street conversion of Homer, Cambie, Georgia and Beatty
- Kingsway and Knight intersection, street and pedestrian improvements
- Greenways – various locations

- Downtown Street Car planning & development
- Street Beautification – various locations
- Arterial improvements - Clark/Knight Corridor safety and livability improvements
- West Broadway Bus Bulges
- Broadway Station - Transit and pedestrian improvements
- Pedestrians - Curb Ramp Program and sidewalk improvements