MEMORANDUM

March 7, 2014

TO: Mayor and Council

CC: Mukhtar Latif, Chief Housing Officer
Sadhu Johnston, Deputy City Manager
Janice MacKenzie, City Clerk
Kevin Quinlan, Director, Policy and Communications, Mayor's Office
Lynda Graves, Manager, Administration Services, City Manager's Office
Mike Magee, Chief of Staff, Mayor's Office
Rena Kendall-Craden, Director, Communications
Brian Jackson, General Manager, Planning and Development Services
Brenda Prosken, General Manager, Community Services
Bill Aujla, General Manager, Real Estate and Facilities Management
Abi Bond, Assistant Director of Housing Policy
Kevin McNaney, Assistant Director, Planning and Development Services
Tom Wanklin, Senior Planner, DTES Neighbourhoods Group

FROM: Penny Ballem, City Manager

SUBJECT: Downtown Eastside Local Area Plan – Approach to Achievement of Social Housing Goals

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This memo and the related attachment (Attachment A) provides Council with information regarding the background analysis and assumptions behind the social housing goals conducted during the preparation of the Downtown Eastside Local Area Plan (DTES LAP).

Background

The development of a renewed strategy to implement the DTES Housing Plan (2005)[1] was identified as a priority of the planning work that led to the DTES LAP[2]. This included careful review of all existing zoning bylaws, policies and guidelines with respect to how they could enable the overall goals outlined in the 2005 Housing Plan.

Each neighbourhood in the DTES plays a unique role in providing a range of housing types in the area, with an overall longstanding vision of the DTES being a mixed-income community.

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[1] See DTES Housing Plan (2005) online: http://former.vancouver.ca/commsvcs/guidelines/D012.pdf

[2] On January 20, 2011 Council established the LAP to *"enhance and accelerate a DTES Local Area Planning Process and a strategy to implement the Council's 2005 DTES Housing Plan"*.

The DTES Community Plan coming before Council on 12 March 2014 reflects the analysis of the required approach needed to achieve the goals set out in the 2005 Housing Plan. The goals of the 2005 Housing Plan had a specific focus on the housing needs of the low income community in the DTES and the housing recommendations in the 2014 DTES Community Plan are built on key assumptions which result from careful analysis by staff and external consultants as to the conditions for success in achieving these and other important housing goals.

The Downtown Eastside Oppenheimer District (DEOD) and the industrial 'let go' areas of Hastings East (M1) and Kiwassa (I2) have been identified as key areas to achieve social housing as land values are relatively low compared to other parts of the DTES.

The 2014 DTES Community Plan provides a balanced approach to addressing the key housing challenges faced by low income residents in the Downtown Eastside, enabling access to affordable homes to those on modest incomes, whilst creating a vibrant, sustainable environment for local business.

Throughout the work of the Plan, there has been detailed analysis of the key assumptions and capacity in these districts in regard to the achieving the housing goals, particularly as it relates to social housing needs and goals. Coriolis have been engaged by the City and have done extensive analysis, testing the assumptions and projecting the scenarios resulting from these assumptions under different economic conditions. It is clear from all the work done that there will be a requirement for the local communities, developers, non-profits, municipal and senior levels of government to work together to achieve the desired outcomes as quickly as possible. Based on the extensive work done, staff have confidence that the housing goals in the DTES Community Plan goals are achievable on the understanding that projects will require a sophisticated approach, in some cases additional form of financial support, and the involvement of multiple partners.

A summary of the work done by Coriolis is attached as Appendix A in the form of a summary memo to the Chief Housing Officer. I would direct your attention particularly to Section 1.3 entitled "Key Assumptions" as these assumptions are the foundation of our approach, particularly where it relates to the leveraging of social housing in the DTES and particularly the DEOD.

Please don't hesitate to call the Chief Housing Officer, Mukhtar Latif, the Director of Planning, Brian Jackson, or myself if you have any questions.

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M E M O R A N D U M

CORIOLIS CONSULTING CORP.

DATE: 28 February 2014

TO: Mukhtar Latif, Chief Housing Officer, City of Vancouver

FROM: Blair Erb, Coriolis Consulting Corp.

RE: **Summary of Financial Analysis for DTES Social Housing Scenarios**

1.0 Introduction

In 2012, the City retained Coriolis Consulting Corp. to provide preliminary market and financial inputs to the Local Area Plan (LAP) process for the Downtown Eastside (DTES). Our initial analysis examined the financial viability of development at sites throughout the LAP study area.

During 2013, as further input to the planning process, the City asked us to evaluate whether it would be financially viable for developers to provide specific amounts of new turnkey social housing as part of redevelopment projects in four specific portions of the LAP study area:

1. DEOD Subarea 1, which is located along East Hastings between Heatley Avenue and Carrall Street and along Main Street between East Hastings and Alexander Street.
2. DEOD Subarea 4, which is located along Alexander Street between Heatley Avenue and Main Street as well as Powell Street between Heatley Avenue and Princess Avenue.
3. The portion of the study area currently zoned M-1 along East Hastings between Heatley Avenue and Clark Drive.
4. The portion of the study area currently zoned I-2 along Raymur Avenue between East Pender Street and Venables Street.

The purpose of this memo is to summarize the main findings of our financial analysis for the density and affordable housing scenarios that the City asked us to analyze for sites in the existing DEOD, M-1 and I-2 districts.

1.1 Affordable Housing and Density Scenarios Analyzed

During 2013, the City asked us to analyze a variety of redevelopment and affordable housing scenarios for sites in the four different zoning districts.

This memo focuses on the most recent density and affordable housing scenarios that the City asked us to analyze. These density and affordable housing scenarios can be summarized as follows.

1. For sites that are currently zoned DEOD and located in Subarea 1:
    - A maximum permitted density of 5.0 to 8.0 FSR.
    - Commercial floorspace at grade with residential units above.
    - Residential unit mix of 60% non-market housing and 40% market rental.
    - No strata residential units.
    - Average non-market unit sizes of 250 sq.ft. net rentable.

- Average market rental unit sizes of 600 sq.ft. net rentable.

2. For sites that are currently zoned DEOD and located in Subarea 4:
   - A maximum permitted density of 2.5 FSR.
   - Commercial floorspace at grade with residential units above.
   - Residential unit mix of 60% non-market housing and 40% market rental.
   - No strata residential units.
   - Average non-market unit sizes of 250 sq.ft. net rentable.
   - Average market rental unit sizes of 600 sq.ft. net rentable.
3. For sites in the LAP study area that are currently zoned M-1:
   - A maximum permitted density of 4.5 to 5.5 FSR.
   - Commercial floorspace at grade with residential units above.
   - Residential unit mix of 25% non-market housing and 75% strata.
   - Average non-market unit sizes of 320 sq.ft. net rentable.
4. For sites in the LAP study area that are currently zoned I-2:
   - A maximum permitted density of 2.5 to 3.0 FSR.
   - No requirement for commercial space.
   - Residential unit mix of 20% non-market housing and 80% strata.
   - Average non-market unit sizes of 600 to 805 sq.ft. net rentable.

1.2 Approach

There is very little vacant land in the DTES, so new development will occur mainly through redevelopment of existing properties. In order for redevelopment to be financially viable, the land value supported by the redevelopment project needs to exceed the property value under existing use and zoning.

Our analysis compares the land value supported by various redevelopment scenarios (including the cost of constructing the social housing) with the value of the site under existing use and zoning to determine whether redevelopment at the assumed density and social housing requirement will be financially viable from a developer's perspective.

Our approach included the following main steps:

1. In consultation with City staff, we identified different case study sites for our analysis. The case study sites that were selected include sites from each of the different zoning districts (DEOD, M-1 and I-2) and focus on sites that are currently improved with older low density improvements so that the existing property value is mainly land value, not the additional value created by the improvements.
2. For each site and development scenario we completed the following steps:
   a) We estimated the market value of the property under existing use and zoning.
   b) We estimated the maximum land value supported by the density and affordable housing scenario, assuming that the completed non-market housing units were transferred by the developer to the City (or a non-profit) at a nominal cost (i.e., $1), the developer holds or sells (to an investor) the market rental units and commercial space, and the developer sells the strata units. In order for the concept to be financially viable, the land value supported by the redevelopment scenario needs to equal or exceed the estimated market value of the property under existing use and zoning and the scenario needs to provide a reasonable return on project costs.

c) If the scenario was not financially viable, we calculated the additional revenue that would need to be generated to the developer from the non-market housing units in order to make the project financially viable.

d) We tested the ability of the non-market units in the scenario to support a mortgage that would generate the required additional revenue (i.e. the amount identified in step c). This step was based on specific assumptions provided by the City about maximum non-market unit rents, non-market unit operating costs and mortgage assumptions.

3. For each of the case study sites that are in the DEOD, the City asked us to analyze the financial viability of redevelopment twice:
   a) First, assuming that the project is developed by a private developer who requires a development management fee and needs to earn a development profit margin on the overall project.
   b) Second, assuming the project is developed by a non-profit that requires a development management fee, but does not require a development profit on the overall project. The financial objective of the non-profit developer would be to break-even on the overall project.
4. For case study sites in the M-1 and I-2 Districts, we analyzed the financial viability of redevelopment under the various density and non-market housing scenarios provided by the City assuming that the project is developed by private developer who needs to earn a development profit margin.

Our analysis focuses on the financial viability of the density and non-market housing scenarios provided by the City. There are numerous other factors which influence the selection of land uses and appropriate densities for intensification including social planning objectives, urban design objectives, existing community character, heritage building retention, transportation requirements, servicing capacity, and the general ability of the area to absorb new population and employment.

We have not completed an evaluation of other factors that should be considered to determine appropriate densities and uses in the DTES.

1.3 Key Assumptions

Our analysis is based on the following key assumptions:

1. Social housing units will be incorporated into projects in a way that minimizes any impacts on the marketability of strata units or the market rental units. Our analysis assumes there is no impact on the sales prices or marketability of any market housing component.
2. New social housing units will be transferred by the developer to the City (or a non-profit housing provider) upon completion in accordance with agreed upon business terms.
3. New market rental units could either be held by the developer or sold at market value.
4. Strata units are sold by the developer at full market value.
5. No DCLs are payable on the social housing units.
6. No DCLs are payable on market rental units that are part of a mixed rental and non-market building (which is the case for the DEOD scenarios).
7. DCLs are payable on strata units, commercial space and rental units in mixed tenure buildings.
8. No off-street parking will be required for non-market units or market rental units in the DEOD.
9. Off-street parking for the social housing and strata units for the M-1 and I-2 sites is based on the City's current parking bylaw requirements. The City indicated that off-street parking may be relaxed from current bylaw requirements in these locations. However, our analysis assumes that parking stalls for

the market component are provided at current bylaw requirements (about 0.9 stalls per strata unit) in order to make the units marketable. Although the inclusion of parking will increase construction costs, it will also increase the marketability and average sales prices for units.

10. Projects are required to achieve LEED Gold certification.
11. For the purpose of estimating the mortgage that could be supported by the non-market units, the non-market unit rents are set at the maximum rent specified by BC Housing's 2013 Housing Income Limit (HILs). The maximum assumed rent for bachelor units is $850 per month, the maximum assumed rent for 1 bedroom units is $950 per month and the maximum rent for 2 bedroom units is $1160 per month. This does not mean that non-market rents will actually be set at these levels as the City and non-market housing providers will likely want to achieve lower rents (at least on a share of the units). However, if rents are lower, it will mean that the supportable mortgage will be lower and that additional grants or other subsidies may need to be provided.
12. Grade level commercial space at mixed-use sites (in the DEOD 1, DEOD 4, M-1 districts) is assumed to be retail and service space. If the grade level space is office, industrial or institutional, it will reduce the financial viability of the redevelopment scenarios as these uses achieve lower lease rates than retail.

Changes to these assumptions will affect the results of the analysis.

2.0 Summary of Findings by District

This section summarizes the main findings of the analysis divided into four parts:

1. Sites in DEOD Subarea 1.
2. Sites in DEOD Subarea 4.
3. Sites in the M-1 District.
4. Sites in the I-2 District.

The results of the analysis should not be interpreted as a recommendation to proceed with the densities and non-market housing requirements identified in this memo. There is a wide variety of other factors that should be considered which influence the selection of land uses, non-market housing requirements, and appropriate densities for the DTES.

2.1 Sites in DEOD Subarea 1

The DEOD Subarea 1 currently allows commercial and residential uses up to 1.0 FSR with the potential to bonus to a maximum density of 5.0 FSR if 20% of the floorspace over 1.0 FSR is provided as social housing.

We analyzed redevelopment in DEOD Subarea 1 with 60% of the units as non-market units and 40% of the units as market rental units. The key findings of our financial analysis can summarized as follows:

1. Under existing DEOD zoning and social housing requirements, it appears that very few DEOD 1 sites are financially viable for redevelopment. Most properties in this district are more valuable under existing commercial and/or residential use (as income-producing properties) than as redevelopment sites.
2. Under the proposed density and social housing scenario, redevelopment is not financially viable if turnkey non-market units are provided by the developer to the City (or a non-profit) at a nominal price.

Developers will not proceed under this scenario if sufficient revenue cannot be generated by the non-market component to make the overall project financially viable.

3. The amount of the funding gap that will need to be addressed will depend on whether the project is built by a private developer or a non-profit developer. The funding gap will need to be met by the City, other levels of government, or a non-profit housing provider.
4. Part of any required funding for the non-market component can be met by obtaining a mortgage on the non-market units. The amount of the supportable mortgage will depend on the mortgage terms and the rents on the non-market units.

Our analysis indicates that the 60% non-market/40% rental concept in the existing DEOD 1 could work for a private developer under very specific circumstances:

1. The developer would need to acquire a development site at existing vacant DEOD 1 land value.
2. The City would need to agree on an average non-market unit size of 250 sq.ft. or less.
3. The project would need to be constructed during a strong rental market. Currently, the market rental portion assumed in the development scenario performs well financially due to favourable market conditions in the Vancouver rental investment market (i.e. low cap rates, low borrowing costs, low vacancy, increasing rents). If rental market conditions deteriorate, then the financial performance of the market rental component (and the overall project) will be less attractive.
4. The market rental units (40% of the units) would need to be rented at full market rents.
5. The City (or other levels of government or a non-profit) would need to purchase the non-market units at a price that makes the development viable.

It is possible that non-profit developers will be interested in pursuing projects in the DEOD with 60% non-market units and 40% market rental. Our analysis indicates that the 60%-40% concept could work for a non-profit developer under specific circumstances:

1. The non-profit would need to acquire a development site at existing vacant DEOD 1 land value.
2. The City would need to agree on an average non-market unit size of 250 sq.ft. or less.
3. The project would need to be constructed during a strong rental market (to ensure the market component performs well).
4. The market rental units (40% of the units) would need to be rented at full market rents.
5. The City would need to agree on a rent structure for the non-market units that can support a sufficient mortgage.
6. If the City wants the non-market unit rents to be reduced, the City (or other level of government) would need to provide an additional grant or subsidy to the non-profit developer.

2.2 Sites in DEOD Subarea 4

The DEOD Subarea 4 currently allows commercial and residential uses at 1.0 FSR with the potential to bonus to a maximum density of 2.5 FSR if 20% of the floorspace over 1.0 FSR is provided as social housing. The same density and social housing requirement applies to the adjacent DEOD Subareas 2 and 3 so the results of our analysis also apply to these subareas.

We analyzed redevelopment in DEOD Subarea 4 assuming a maximum density of 2.5 FSR with 60% of the units as non-market units and 40% of the units as market rental units. The key findings of our analysis can be summarized as follows:

1. Under existing DEOD zoning and social housing requirements, it appears that vacant DEOD 4 sites (or sites with very low value improvements) are currently financially viable for redevelopment. Therefore, some owners and developers may be interested in proceeding with development in this subarea under current zoning and development regulations.
2. Under the proposed density and social housing scenario, redevelopment is not financially viable if turnkey non-market units are provided by the developer to the City (or a non-profit) at a nominal price. Developers will not proceed under this scenario if sufficient revenue cannot be generated by the non-market component to make the overall project financially viable.
3. The amount of the funding gap that will need to be addressed will depend on whether the project is built by a private developer or a non-profit developer. The funding gap will need to be met by the City, other levels of government, or a non-profit housing provider.
4. Part of any required funding for the non-market component can be met by obtaining a mortgage on the non-market units. The amount of the supportable mortgage will depend on the mortgage terms and the rents on the non-market units.

Our analysis indicates that the 60% non-market/40% rental concept in the existing DEOD 4 could work for a private developer under very specific circumstances:

1. The developer would need to acquire a development site at existing vacant DEOD 4 land value.
2. The City would need to agree on an average non-market unit size of 250 sq.ft. or less.
3. The project would need to be constructed during a strong rental market.
4. The market rental units (40% of the units) would need to be rented at full market rents.
5. The City (or other levels of government or a non-profit) would need to purchase the non-market units at a price that makes the development viable.

It is possible that non-profit developers will be interested in pursuing projects in the DEOD 4 with 60% non-market units and 40% market rental. Our analysis indicates that the 60%-40% concept could work for a non-profit developer under specific circumstances:

1. The non-profit would need to acquire a development site at existing vacant DEOD 4 land value.
2. The City would need to agree on an average non-market unit size of 250 sq.ft. or less.
3. The project would need to be constructed during a strong rental market.
4. The market rental units (40% of the units) would need to be rented at full market rents.
5. The City would need to agree on a rent structure for the non-market units that can support a sufficient mortgage.
6. If the City wants the non-market unit rents to be reduced, the City (or other level of government) would need to provide an additional grant or subsidy to the non-profit developer.

2.3 Sites in the M-1 District

The M-1 District permits a wide range of commercial and industrial uses, but it does not permit multifamily housing. The maximum permitted density in the M-1 District is 5.0 FSR and the maximum height is 100 feet. Most sites are improved with single storey or two storey commercial/service buildings so existing property values are often higher than vacant M-1 industrial land value. However, we focused our analysis on sites that have improvements which make minimal contribution to overall property value.

We analyzed redevelopment of sites in the M-1 portion of the LAP study area assuming 25% of the units are non-market units and 75% of the units are strata units. The non-market units are assumed to average 320 sq.ft. net each. We evaluated density scenarios ranging from 4.5 FSR to 5.5 FSR. It is our understanding that some sites in the M-1 area could be considered for higher or lower densities.

The key findings of our analysis can be summarized as follows:

1. If turnkey non-market units are provided by the developer to the City (or a non-profit) at a nominal price, the redevelopment scenarios that we tested are not financially viable (assuming 320 sq.ft. per non-market unit). Developers will not proceed with projects if sufficient revenue cannot be generated by the non-market component to make the overall project financially viable.
2. The amount of the funding gap will that will need to be addressed will depend on the overall density that is approved. Any funding gap will need to be met by the City, other levels of government, or a non-profit housing provider.
3. Part of any required funding can be met by obtaining a mortgage on the non-market units. The amount of the supportable mortgage will depend on the mortgage terms and the rents on the non-market units.

Based on our analysis, it will be financially viable for private developers to pursue redevelopment of M-1 properties at 4.5 FSR to 5.5 FSR with 25% non-market units and 75% strata units if:

1. The developer can acquire a development site at existing vacant M-1 land value.
2. The City agrees on a maximum average non-market unit size of 320 sq.ft.
3. The City (or other levels of government or a non-profit) purchase the non-market units at a price that makes the development viable.

2.4 Sites in the I-2 District

The I-2 District permits a wide range of commercial and industrial uses, but it does not permit multifamily housing. The maximum permitted density in the I-2 District is 3.0 FSR and the maximum height is 60 feet. Most I-2 sites in the study area are improved with single storey or two storey industrial buildings so existing property values are often higher than vacant industrial I-2 land value. However, we focused our analysis on sites that have improvements which make minimal contribution to overall property value.

We analyzed redevelopment of sites in the I-2 portion of the LAP study area assuming a maximum density of 3.0 FSR with 20% of the units as non-market units and 80% as strata units. We evaluated different average non-market unit size scenarios, ranging from 600 sq.ft. to 805 sq.ft. net.

The key findings of our financial analysis can be summarized as follows:

1. If turnkey non-market units are required to be provided by the developer to the City (or a non-profit) at a nominal price, then redevelopment will be financially viable if the non-market units average 600 sq.ft. (or less) and the developer acquires a site at existing I-2 land value.
2. If turnkey non-market units are provided by the developer to the City (or a non-profit) at a nominal price, this redevelopment scenario is not financially viable if the average unit size is larger than about 600 sq.ft. At the larger non-market unit size, developers will not proceed with projects if sufficient revenue cannot be generated by the non-market component to make the overall project financially viable.
3. The business terms for the non-market units that could make this redevelopment scenario financially viable vary depending on the assumed size of the non-market units:

- If the non-market units average 600 sq.ft. or less, then no payment will be required from the City (or a non-profit) to make the project financially viable. The non-market units could be provided to the City at a nominal cost.
- If the average non-market unit size is larger than about 600 sq.ft., then the City (or a non-profit housing provider) would need to purchase the non-market units from the private developer at a value that makes the overall development financially viable.

4. Part of any required funding can be met by obtaining a mortgage on the non-market units. The amount of the supportable mortgage will depend on the mortgage terms and the rents on the non-market units.

Based on our analysis, it will be financially viable for private developers to pursue redevelopment of I-2 properties with 20% non-market units and 80% strata units if developers acquire sites at existing I-2 land value. Depending on the size of the non-market units and the approved density, it could be necessary for the City to purchase the non-market units at a value that makes redevelopment financially viable.