Staff Report

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REPORT TO: **Community and Infrastructure Services Committee**

DATE OF MEETING: **June 8, 2022**

SUBMITTED BY: **Rosa Bustamante, Director of Planning, 519-741-2200 ext. 7319**

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WARD(S) INVOLVED: **ALL**

DATE OF REPORT: **May 27, 2022**

REPORT NO.: **DSD-2022-281**

SUBJECT: **Growth Related Funding Tools – Cumulative Impact Assessment**

RECOMMENDATION:

That Report DSD-2022-281 regarding Growth Related Funding Tools – Cumulative Impact Assessment, be received.

REPORT HIGHLIGHTS:

- The purpose of this report is to present Council with the findings of the Cumulative Impact Assessment prepared by N. Barry Lyon Consultants (NBLC) to inform Council's consideration of new or updated Development Charges, Park Dedication, Community Benefits Charges, and Inclusionary Zoning.
- Key findings:
    - The NBLC report found that the funding tools in totality generally result in manageable impacts to proformas in the strong Downtown residential market, with more significant impacts on high-rise development in other locations in Kitchener.
    - The tools impact high rise and rental projects most significantly.
    - A transition period for new fees or policies is critical to mitigating impacts.
    - The recommended Development Charges and Parkland Dedication by-laws incorporate most of the Study's recommendations to mitigate impact on development proformas, risks to housing supply and associated upward pressure on housing prices.
    - In developing these tools, staff have sought to mitigate impacts on development proformas while providing for the infrastructure, parks and city services required to support vibrant complete communities.
- Staff engaged members of the development industry in preparing this report
- This report supports the delivery of core services.

BACKGROUND:

The City is in the process of developing new or updated fees that support growth. Development Charges (DCs), Community Benefits Charges (CBCs), Park Dedication and Inclusionary Zoning (IZ) are all being considered in the next two years and have the possibility of impacting development trends and housing affordability. A new Development Charges By-law was considered by Council on May 30, 2022. Committee of Council will consider and discuss the “Spaces” component of Places and Spaces, a new parks and open space strategy for Kitchener together with a new Park Dedication By-law on June 8. Consideration of CBCs and IZ are in progress with updates to Council anticipated in 2023.

To better understand the financial implications of the above-mentioned fees on development proformas, the City retained N. Barry Lyon Consultants (NBLC) Land Economists to analyse their cumulative impacts.

REPORT:

The NBLC report (Attachment A) uses an industry standard residual land value (RLV) approach to test likely impacts of fee and policy combinations on a set of prototypical proformas that vary in location and housing form. This approach and methodology includes the following important characteristics:

- The costs of increased fees cannot easily be passed onto residents through higher prices because developers are already pricing units as high as the market will bear.
- The model used in the analysis assumes that developer profits cannot be compressed. Without sufficient profit, developers will not be motivated to build, and banks will not provide financing.
- Based on the above, it is concluded that increased fees and charges will put downward pressure on land value.
- If land value is compressed too much, a residential redevelopment project cannot displace the existing land use and will not proceed.
- Reducing housing supply can put upward pressure on housing prices.
- This analysis does not capture all possible developer motivations. Long-term landowners or those that self-finance may continue to develop despite challenges to the prototypical proformas.

Key findings of the report are:

- The proposed DC rates will have a relatively small impact on project viability.
- Although the City has yet to determine if it will implement CBCs, a 4% of land value charge (the maximum permitted in legislation) would have relatively small impacts on project viability.
- Generally, high-rise apartments, rental projects, and areas outside of Downtown are expected to be most impacted by the proposed fees.
- The overall impact of the proposed Park Dedication By-Law could potentially push down land values by 11% in the Downtown example and 35% in central neighbourhoods. Impacts would be much more significant without the proposed $11,862 per unit cap. This fee increase is a one-time adjustment to address a 12-year park dedication value stagnation.
- An example Inclusionary Zoning policy that requires 5% of units to be affordable could further depress land values by 16% at the Downtown test site and by half in central neighbourhoods.

- The cumulative impacts of all new policies could impact land values by 25%-90% depending on location and built form.
- A transition period to the new fee/policy regime is crucial to mitigating impacts to project viability.
- Fees should be tailored to support higher density development in weaker market areas.
- Park dedication impacts could be mitigated through site specific appraisals, area-specific rates, on and offsite land dedication, and a graduated park dedication cap.
- The impact of inclusionary zoning could be mitigated through reduced affordability requirements in weaker markets and offsets such as increases in height and density permissions, reduced parking requirements, fee waivers and/or grants.
- All fees and policies should be reviewed regularly to respond to market conditions.

Staff have reviewed and considered the NBLC report and provide the following additional context for Council's consideration:

- The proposed DC by-law shapes incentives to help support development in Central Neighbourhoods.
- The current draft Park Dedication By-Law responds to the recommendations by:
    - Capping CIL of park dedication at a maximum of $11,862 per unit
    - Providing a transition for existing development applications
    - Providing for on and offsite land dedication and site specific appraisals
- Reductions for rental buildings, and area-specific rates are not included in the draft by-law (due to limited comparable data for high density sites outside Downtown)
- Inclusionary Zoning (IZ) will have the greatest impact on proformas and will be the last tool to be introduced, which will potentially be challenging to implement in all areas except for Downtown in the short and medium term. However, it should be noted that the City of Kitchener has used other policy support tools to advance supportive and affordable housing in these areas.
- Kitchener should have reasonable expectations regarding the amount of affordable units that IZ can deliver. Continued investment by all levels of government in affordable housing is required to achieve broad affordable housing objectives.
- Many potential offsets to achieve IZ in weaker markets either have financial implications to the tax base, or may not have significant value for developers.
- The potential implications of new and updated growth-related fees on development, including in Major Transit Station Areas east of Downtown, will be closely monitored to understand whether additional mitigation measures are needed. Any mitigation measures may require future Council direction. At this time it is unclear if impacts forecasted will materialize and whether further mitigation measures are warranted.
- Concerns remain with the premise that increased fees will put downward pressure on land rather than upward pressure on unit prices and rents.
- The NBLC report uses theoretical projects, based on prototypes, and the results are very sensitive to a set of assumptions. It is therefore not a good predictor of actual land transaction prices. It does however remain a valuable way to evaluate the potential impact of new fees and policies.
- The residual land values in the report are higher than observed actual transactions and listings. This would imply a greater capacity for the development industry to absorb additional fees than suggested by the NBLC report, especially Downtown.

- There is less certainty regarding valuation of high-density development outside of Downtown with limited comparable data to rely on.

<u>Conclusion</u>
Increasing hard costs and the potential for a slow down in unit production or decrease in unit prices are expected to put pressure on development proformas in the near term. While comparable with other municipalities, the City's proposed fee regime may challenge high and medium density development, particularly outside of the Downtown market. This requires a balanced consideration of DCs, CBCs, Cash-in-lieu of Parkland and IZ on one hand, and development viability and the resultant housing supply and overall affordability on the other. Higher taxes could provide some relief by shifting costs from developers to the existing tax base and would go against the principle of growth paying for growth.

The proposed Park Dedication and Development Charges By-Laws have incorporated many of the NBLC study's recommendations to mitigate impacts on developer proformas, while providing services, infrastructure and parkland needed for thriving and complete communities. Market realities will challenge the ability to achieve a significant number of affordable units through Inclusionary Zoning in the medium term, especially outside of the Downtown.

STRATEGIC PLAN ALIGNMENT:
This report supports the delivery of core services.

FINANCIAL IMPLICATIONS:
There are no financial implications to this report. This report has been used to inform the development of updates to Kitchener's DC and, Park Dedication By-laws and will be used to inform any Community Benefits Charges and IZ program in the future.

COMMUNITY ENGAGEMENT:
INFORM – This report has been posted to the City's website with the agenda in advance of the Council / Committee meeting.

CONSULT - Staff and NBLC presented the report findings to the Waterloo Region Homebuilders' Kitchener Development Liaison Committee (KDLC), Momentum and IN8 developments in May 2022. Key comments from these groups are:

- A transition period to the new fee regime is critical.
- The vast majority of developers said that increased fees would be passed onto consumers in the form of higher unit prices and rents.
- Medium density development will be further challenged by the proposed fees.
- Profits cannot be compressed. As such, any fee increase may be passed on, in whole or in part to purchasers/renters.
- Developers may respond by delaying projects, building smaller units in taller buildings and/or seek lower architectural design.
- The housing market has weakened in the last 30 days making the introduction of fees more challenging,

More details of these meetings are included in Attachment B.

PREVIOUS REPORTS/AUTHORITIES:
There are no previous reports/authorities related to this matter

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ATTACHMENTS:
Attachment A – NBLC Report - Proposed Municipal Charges and Fees for Residential Development – Evaluation of Potential Impacts (May 2022)
Attachment B – Development industry feedback on NBLC report