

November 11, 2022

To Our Development Charge Clients:

Re: Assessment of Bill 23 (*More Homes Built Faster Act*) – Development Charges

On behalf of our many municipal clients, we are continuing to provide the most up-to-date information on the proposed changes to the *Development Charges Act* (D.C.A.) as proposed by Bill 23 (*More Homes Built Faster Act*). As identified in our October 31, 2022 letter to you, our firm is providing an evaluation of the proposed changes to the D.C.A. along with potential impacts arising from these changes. The following comments will be included in our formal response to the Province, which we anticipate presenting to the Standing Committee on Heritage, Infrastructure and Cultural Policy next week.

1. Overview Commentary

The Province has introduced Bill 23 with the following objective: *“This plan is part of a long-term strategy to increase housing supply and provide attainable housing options for hardworking Ontarians and their families.”* The Province’s plan is to address the housing crisis by targeting the creation of 1.5 million homes over the next 10 years. To implement this plan, Bill 23 introduces a number of changes to the D.C.A., along with nine other Acts including the *Planning Act*, which seek to increase the supply of housing.

As discussed later in this letter, there are proposed changes to the D.C.A. which we would anticipate may limit the future supply of housing units. For urban growth to occur, water and wastewater services must be in place before building permits can be issued for housing. Most municipalities assume the risk of constructing this infrastructure and wait for development to occur. Currently, 26% of municipalities providing water/ wastewater services are carrying negative development charge (D.C.) reserve fund balances for these services¹ and many others are carrying significant growth-related debt. In addition to the current burdens, Bill 23 proposes to:

- Phase in any new by-laws over five years which, on average, would reduce D.C. revenues by approximately 10%;
- Introduce new exemptions which would provide a potential loss of 10-15% of the D.C. funding;

¹ Based on 2020 Financial Information Return data.



- Remove funding of water/wastewater master plans and environmental assessments which provide for specific planning and approval of infrastructure; and
- Make changes to the *Planning Act* that would minimize upper-tier planning in two-tier systems where the upper-tier municipality provides water/wastewater servicing. This disjointing between planning approvals and timing/location of infrastructure construction may result in inefficient servicing, further limiting the supply of serviced land.

The loss in funding noted above must then be passed on to existing rate payers. This comes at a time when municipalities must implement asset management plans under the *Infrastructure for Jobs and Prosperity Act* to maintain existing infrastructure. Significant annual rate increases may then limit funding to the capital budget and hence delay construction of growth-related infrastructure needed to expand the supply of serviced land.

The above-noted D.C.A. changes will also impact other services in a similar manner.

The removal of municipal housing as an eligible service will reduce municipalities' participation in creating assisted/affordable housing units. Based on present D.C. by-laws in place, over \$2.2 billion in net growth-related expenditures providing for over 47,000 units (or 3.1% of the Province's 1.5 million housing target) would be impacted by this change.

The proposed changes to the D.C.A. result in a subsidization of growth by the existing rate/taxpayer by reducing the D.C.s payable. Over the past 33 years, there have been changes made to the D.C.A. which have similarly reduced the D.C.s payable by development. These historical reductions have not resulted in a decrease in housing prices; hence, it is difficult to relate the loss of needed infrastructure funding to affordable housing. The increases in water/wastewater rates and property taxes would directly impact housing affordability for the existing rate/taxpayer.

While the merits of affordable housing initiatives are not in question, they may be best achieved by participation at local, provincial, and federal levels. Should the reduction in D.C.s be determined to be a positive contributor to increasing the amount of affordable housing, then grants and subsidies should be provided to municipalities to fund the growth-related infrastructure and thereby reduce the D.C. In this way, the required funding is in place to create the land supply. Alternatively, other funding options could be made available to municipalities as an offset (e.g., the Association of Municipalities of Ontario (AMO) has suggested municipalities have access to 1% of HST, consideration of a special Land Transfer Tax, etc.).

A summary of the proposed D.C.A. changes, along with our firm's commentary, is provided below.



2. Changes to the D.C.A.

2.1 Additional Residential Unit Exemption: The rules for these exemptions are now provided in the D.C.A., rather than the regulations and are summarized as follows:

- Exemption for residential units in existing rental residential buildings – For rental residential buildings with four or more residential units, the greater of one unit or 1% of the existing residential units will be exempt from D.C.
- Exemption for additional residential units in existing and new residential buildings
 - The following developments will be exempt from a D.C.:
 - A second unit in a detached, semi-detached, or rowhouse if all buildings and ancillary structures cumulatively contain no more than one residential unit;
 - A third unit in a detached, semi-detached, or rowhouse if no buildings or ancillary structures contain any residential units; and
 - One residential unit in a building or structure ancillary to a detached, semi-detached, or rowhouse on a parcel of urban land, if the detached, semi-detached, or rowhouse contains no more than two residential units and no other buildings or ancillary structures contain any residential units.

Analysis/Commentary

- For existing single-family homes, this change will not have an impact. For other existing low/medium-density units and for all new units, however, this allowance of a third additional unit that will be exempt from D.C.s adds a further revenue loss burden to municipalities to finance infrastructure. This is of greatest concern for water and wastewater services where each additional unit will require additional capacity in water and wastewater treatment plants. This additional exemption will cause a reduction in D.C.s and hence will require funding by water and wastewater rates.
- Other services, such as transit and active transportation, will also be impacted as increased density will create a greater need for these services, and without an offsetting revenue to fund the capital needs, service levels provided may be reduced in the future.

2.2 Removal of Housing as an Eligible D.C. Service: Housing services would be removed as an eligible service. Municipalities with by-laws that include a charge for housing services can no longer collect for this service once subsection 2 (2) of Schedule 3 of the Bill comes into force.

Analysis/Commentary

- The removal of housing services will reduce municipalities' participation in creating assisted/affordable housing units and/or put further burden on municipal



taxpayers. This service seeks to construct municipal affordable housing for growing communities. The removal of this service could reduce the number of affordable units being constructed over the next ten years, if the municipalities can no longer afford the construction. Based on present D.C. by-laws in place, over \$2.2 billion in net growth-related expenditures providing for over 47,000 additional units (or 3.1% of the Province's 1.5 million housing target) would be impacted by this change.

2.3 New Statutory Exemptions: Affordable units, attainable units, inclusionary zoning units and non-profit housing developments will be exempt from the payment of D.C.s, as follows:

- Affordable Rental Units: Where rent is no more than 80% of the average market rent as defined by a new bulletin published by the Ministry of Municipal Affairs and Housing.
- Affordable Owned Units: Where the price of the unit is no more than 80% of the average purchase price as defined by a new bulletin published by the Ministry of Municipal Affairs and Housing.
- Attainable Units: Excludes affordable units and rental units; will be defined as prescribed development or class of development and sold to a person who is at “arm’s length” from the seller.
 - Note: for affordable and attainable units, the municipality shall enter into an agreement that ensures the unit remains affordable or attainable for 25 years.
- Inclusionary Zoning Units: Affordable housing units required under inclusionary zoning by-laws will be exempt from a D.C.
- Non-Profit Housing: Non-profit housing units are exempt from D.C. instalment payments due after this section comes into force.

Analysis/Commentary

- While this is an admirable goal to create additional affordable housing units, further D.C. exemptions will continue to provide additional financial burdens on municipalities to fund these exemptions without the financial participation of senior levels of government.
- The definition of “attainable” is unclear, as this has not yet been defined in the regulations.
- Municipalities will have to enter into agreements to ensure these units remain affordable and attainable over a period of time which will increase the administrative burden (and costs) on municipalities. These administrative burdens will be cumbersome and will need to be monitored by both the upper-tier and lower-tier municipalities.
- It is unclear whether the bulletin provided by the Province will be specific to each municipality, each County/Region, or Province-wide. Due to the disparity in



incomes across Ontario, affordability will vary significantly across these jurisdictions. Even within an individual municipality, there can be disparity in the average market rents and average market purchase prices.

2.4 Historical Level of Service: Currently, the increase in need for service is limited by the average historical level of service calculated over the ten year period preceding the preparation of the D.C. background study. This average will be extended to the historical 15-year period.

Analysis/Commentary

- For municipalities experiencing significant growth in recent years, this may reduce the level of service cap, and the correspondingly D.C. recovery. For many other municipalities seeking to save for new facilities, this may reduce their overall recoveries and potentially delay construction.
- This further limits municipalities in their ability to finance growth-related capital expenditures where debt funding was recently issued. Given that municipalities are also legislated to address asset management requirements, their ability to incur further debt may be constrained.

2.5 Capital Costs: The definition of capital costs may be revised to prescribe services for which land or an interest in land will be restricted. Additionally, costs of studies, including the preparation of the D.C. background study, will no longer be an eligible capital cost for D.C. funding.

Analysis/Commentary

- Land
 - Land costs are proposed to be removed from the list of eligible costs for certain services (to be prescribed later). Land represents a significant cost for some municipalities in the purchase of property to provide services to new residents. This is a cost required due to growth and should be funded by new development, if not dedicated by development directly.
- Studies
 - Studies, such as Official Plans and Secondary Plans, are required to establish when, where, and how a municipality will grow. These growth-related studies should remain funded by growth.
 - Master Plans and environmental assessments are required to understand the servicing needs development will place on hard infrastructure such as water, wastewater, stormwater, and roads. These studies are necessary to inform the servicing required to establish the supply of lands for development; without these servicing studies, additional development cannot proceed. This would restrict the supply of serviced land and would be counter to the Province's intent to create additional housing units.



2.6 Mandatory Phase-in of a D.C.: For all D.C. by-laws passed after June 1, 2022, the charge must be phased-in annually over the first five years the by-law is in force, as follows:

- Year 1 – 80% of the maximum charge;
- Year 2 – 85% of the maximum charge;
- Year 3 – 90% of the maximum charge;
- Year 4 – 95% of the maximum charge; and
- Year 5 to expiry – 100% of the maximum charge.

Note: for a D.C. by-law passed on or after June 1, 2022, the phase-in provisions would only apply to D.C.s payable on or after the day subsection 5 (7) of Schedule 3 of the Bill comes into force (i.e., no refunds are required for a D.C. payable between June 1, 2022 and the day the Bill receives Royal Assent). The phased-in charges also apply with respect to the determination of the charges under section 26.2 of the Act (i.e., eligible site plan and zoning by-law amendment applications).

Analysis/Commentary

- Water, wastewater, stormwater, and roads are essential services for creating land supply for new homes. These expenditures are significant and must be made in advance of growth. As a result, the municipality assumes the investment in the infrastructure and then assumes risk that the economy will remain buoyant enough to allow for the recovery of these costs in a timely manner. Otherwise, these growth-related costs will directly impact the existing rate payer.
- The mandatory phase-in will result in municipalities losing approximately 10% to 15% of revenues over the five-year phase-in period. For services such as water, wastewater, stormwater, and to some extent roads, this will result in the municipality having to fund this shortfall from other sources (i.e., taxes and rates). This may result in: 1) the delay of construction of infrastructure that is required to service new homes; and 2) a negative impact on the tax/rate payer who will have to fund these D.C. revenue losses.
- Growth has increased in communities outside the Greater Toronto Area (G.T.A.) (e.g. municipalities in the outer rim), requiring significant investments in water and wastewater treatment services. Currently, there are several municipalities in the process of negotiating with developing landowners to provide these treatment services. For example, there are two municipalities within the outer rim (one is 10 km from the G.T.A. while the other is 50 km from the G.T.A.) imminently about to enter into developer agreements and award tenders for the servicing of the equivalent of 8,000 single detached units (or up to 20,000 high-density units). This proposed change to the D.C.A. alone will stop the creation of those units due to debt capacity issues and the significant financial impact placed on



ratepayers due to the D.C. funding loss. Given our work throughout the Province, it is expected that there will be many municipalities in similar situations.

- Based on 2020 Financial Information Return (F.I.R.) data, there are 214 municipalities with D.C. reserve funds. Of those, 130 provide water and wastewater services and of those, 34 municipalities (or 26%) are carrying negative water and wastewater reserve fund balances. As a result, it appears many municipalities are already carrying significant burdens in investing in water/wastewater infrastructure to create additional development lands. This proposed change will worsen the problem and, in many cases, significantly delay or inhibit the creation of serviced lands in the future.
- Note that it is unclear how the phase-in provisions will affect amendments to existing D.C. by-laws.

2.7 D.C. By-law Expiry: A D.C. by-law would expire ten years after the day it comes into force. This extends the by-law's life from five years, currently. D.C. by-laws that expire prior to subsection 6 (1) of the Bill coming into force would not be allowed to extend the life of the by-law.

Analysis/Commentary

- The extension of the life of the D.C. by-law would appear to not have an immediate financial impact on municipalities. Due to the recent increases in actual construction costs experienced by municipalities, however, the index used to adjust the D.C. for inflation is not keeping adequate pace (e.g., the most recent D.C. index has increased at 15% over the past year; however, municipalities are experiencing 40%-60% increases in tender prices). As a result, amending the present by-laws to update cost estimates for planned infrastructure would place municipalities in a better financial position.
- As a result of the above, delaying the updating of current D.C. by-laws for five more years would reduce actual D.C. recoveries and place the municipalities at risk of underfunding growth-related expenditures.

2.8 Instalment Payments: Non-profit housing development has been removed from the instalment payment section of the Act (section 26.1), as these units are now exempt from the payment of a D.C.

Analysis/Commentary

- This change is more administrative in nature due to the additional exemption for non-profit housing units.

2.9 Rental Housing Discount: The D.C. payable for rental housing development will be reduced based on the number of bedrooms in each unit as follows:

- Three or more bedrooms – 25% reduction;



- Two bedrooms – 20% reduction; and
- All other bedroom quantities – 15% reduction.

Analysis/Commentary

- Further discounts to D.C.s will place an additional financial burden on municipalities to fund these reductions.
- The discount for rental housing does not appear to have the same requirements as the affordable and attainable exemptions to enter into an agreement for a specified length of time. This means a developer may build a rental development and convert the development (say to a condominium) in the future hence avoiding the full D.C. payment for its increase in need for service.

2.10 Maximum Interest Rate for Instalments and Determination of Charge for Eligible Site Plan and Zoning By-law Amendment Applications: No maximum interest rate was previously prescribed. Under the proposed changes, the maximum interest rate would be set at the average prime rate plus 1%. How the average prime rate is determined is further defined under section 9 of Schedule 3 of the Bill. This maximum interest rate provision would apply to all instalment payments and eligible site plan and zoning by-law amendment applications occurring after section 9 of Schedule 3 of the Bill comes into force.

Analysis/Commentary

- Setting the maximum interest rate at 1%+ the average prime rate appears consistent with the current approach for some municipalities but is a potential reduction for others.
- It appears a municipality can select the adjustment date for which the average prime rate would be calculated.
- The proposed change will require municipalities to change their interest rate policies, or amend their by-laws, as well as increase the administrative burden on municipalities.

2.11 Requirement to Allocate Funds Received: Similar to the requirements for community benefits charges, annually, beginning in 2023, municipalities will be required to spend or allocate at least 60% of the monies in a reserve fund at the beginning of the year for water, wastewater, and services related to a highway. Other services may be prescribed by the regulation.

Analysis/Commentary

- This proposed change appears largely administrative and would not have a financial impact on municipalities. This can be achieved as a schedule as part of the annual capital budget process or can be included as one of the schedules



with the annual D.C. Treasurer Statement. This, however, will increase the administrative burden on municipalities.

2.12 Amendments to Section 44 (Front-ending): This section has been updated to include the new mandatory exemptions for affordable, attainable, and non-profit housing, along with required affordable residential units under inclusionary zoning by-laws.

Analysis/Commentary

- This change is administrative to align with the additional statutory exemptions.

2.13 Amendments to Section 60: Various amendments to this section were required to align the earlier described changes.

Analysis/Commentary

- These changes are administrative in nature.

We will continue to monitor the legislative changes and advise as the Bill proceeds.

Yours very truly,

WATSON & ASSOCIATES ECONOMISTS LTD.

Gary Scandlan, BA, PLE, Managing Partner

Andrew Grunda, MBA, CPA, CMA, Principal

Jamie Cook, MCIP, RPP, PLE, Managing Partner

Peter Simcisko, BA (Hons), MBE, Managing Partner

Sean-Michael Stephen, MBA, Managing Partner

Jack Ammendolia, BES, PLE, Managing Partner