DRAFT REPORT

Town of Wadena

Background Report to the
Development Levy Bylaw

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February 2019

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1 Financial Growth

This background report to the Development Levy Bylaw is being prepared by the Town of Wadena (Town) to establish the principles and basis for the recovery of the municipality's costs for extending municipal services to new development.

The Town recognizes that it has a fiduciary responsibility to the community to manage its financial resources in a responsible manner based upon sound advice. Establishing a basis for assigning direct and indirect costs of infrastructure based upon the relative benefits of this public investment to the parties involved is essential to responsible governance. It also provides an opportunity for the Town to establish a sound financial strategy to guide decisions concerning the timing for construction and financing of new infrastructure required to support community growth.

Preparing a basis for the application of development related levies and fees which is defendable and reflects accurate capital cost projections is essential to a predictable and transparent development process.

Development charges as referred to in this document refer to servicing agreement fees and development levies as defined within *The Planning and Development Act, 2007* (the Act). Development charges provide communities with an opportunity to define the respective roles of public and private investment in financing growth. Sections 169 and 172 of the Act authorize Council to impose a development charge covering all or a part of the capital costs of providing, altering, expanding or upgrading:

- Sewage, water and drainage works
- Roadways and related infrastructure
- Parks
- Recreational facilities.

Often infrastructure provides a benefit to more than one development and, consequently, the cost of developing the infrastructure should be shared by all benefiting developments. The Act distinguishes between infill development and greenfield subdivision. Infill development involves the intensification of land use on an existing subdivided property where the intensification is expected to trigger additional capital costs. Greenfield subdivision represents the subdivision and extension of new services to previously unsubdivided lands. Development levies are typically applied to infill development whereas servicing agreement fees are generally employed in response to new property subdivisions.

All municipal infrastructure contemplated by the Act generally follows a similar life cycle relying on different funding mechanisms to support this life cycle. Development charges relate directly to the construction phase of this life-cycle.

Figure 1-1
Life Cycle Figure

Growth related infrastructure can be separated into two categories as illustrated below:

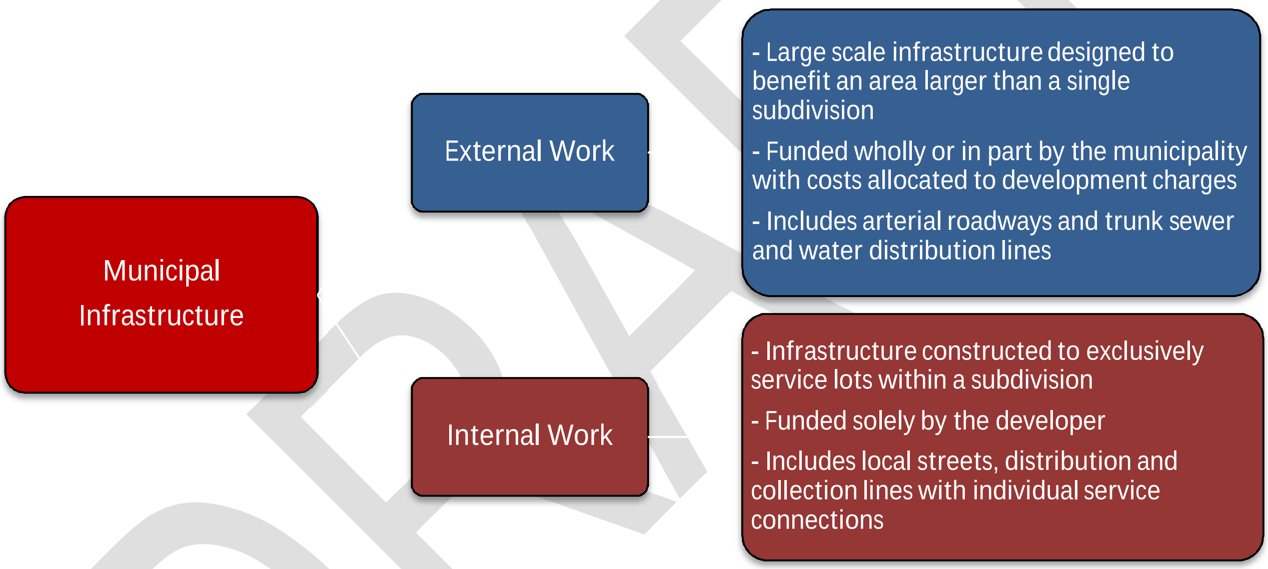

Figure 1-2
Growth Related Infrastructure

For the purposes of this report, it is assumed that internal works will remain the sole responsibility of a private developer and attention will be focused on the various approaches available to Wadena to manage external works.

There are numerous approaches to financing growth related infrastructure. At one end of the spectrum is the municipally centred approach where the municipality finances all the front-end external works and recovers this investment incrementally from developers who are deemed to benefit from these works on a proportionate basis. As new subdivisions occur, each developer is assigned a proportionate responsibility of this municipal investment as a servicing agreement fee or as a condition of a development agreement.

Municipal centred approaches are best suited in the following circumstances:

- Where the spatial extent of a service area is large requiring the party responsible for financing the front-end costs to have significant debt and risk capacity;
- Where the municipality decides to proactively support or incent a certain form of development;
- Where a growth area involves many individual property owners/developers;
- Where the municipality acknowledges that a capital infrastructure project will benefit the existing population by relieving an existing capacity shortfall; and
- Where the local development industry does not have the expertise or experience to front end the costs of major works.

On the other end of the spectrum, a community may take a developer centred approach where the municipality does not take on any direct responsibility for financing growth related infrastructure. In this instance, developers are expected to fund all works using their own resources. This approach is most appropriate:

- Where servicing areas can be compartmentalized allowing for projects to be separated into smaller independent phases, reducing financial obligations and associated risks;
- Where there are a small number of landowners in designated growth areas; and
- Where the municipality has limited financial resources available to support capital infrastructure projects.

Wadena currently utilizes an approach which falls somewhere in the middle of this spectrum by retaining responsibility for financing major water and wastewater treatment systems and community recreational facilities while transferring the obligation for the construction of any linear infrastructure connections to these larger scale systems to individual developers. Under the current approach, developers are held solely responsible for the construction of all sewer and water lines and associated facilities, drainage works and internal and external roadways.

By assigning most of responsibility for constructing external and internal works to the developer, the Town's long-term financial liability is minimized and growth-related infrastructure is predominantly funded through a user pay approach.

2 Funding Sources

The graphic below illustrates the various financial tools available to a municipality to provide the financial resources needed not only to fund growth but also to allow for the operation, maintenance and replacement of these public assets.

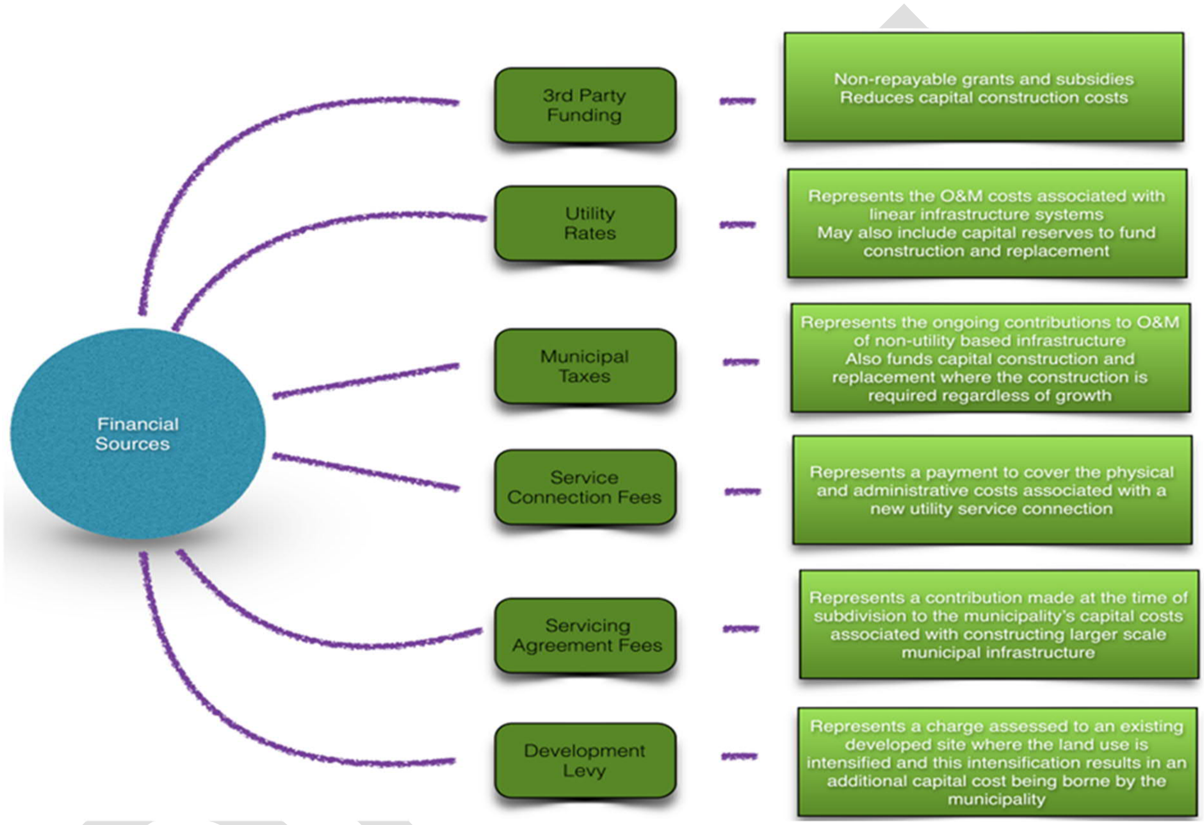

Figure 2-1
Financial Sources Graphic

Investment in new infrastructure to support community growth can draw on any one or all the financial sources represented above. Third party funding, municipal taxes, servicing agreement fees and development levies are most commonly associated with growth related infrastructure projects.

The opportunity exists to incorporate a portion of future capital infrastructure investments for water and wastewater systems and facilities within the Town's utility rates. A utility rate is generally comprised of:

- Administrative costs (wages/salaries/benefits)
- Supply costs (water supply)
- Operation and maintenance costs
- Capital reserves

The Town may assign a portion of any planned capital improvements to the water and wastewater systems to supplement the other growth-related funding sources typically employed and identified above.

By assigning a portion of the planned capital cost for these projects to a utility rate, the Town may establish a consistent source of repayment and a broader funding base for capital projects. Where the utility rate does account for future capital expansion and/or replacement, the Act requires that these funds be used to reduce the overall projected capital cost assigned by the development charges to avoid duplication of funding.

3 Basis for Calculation

Development charges can be calculated and assessed in a variety of ways based upon land use and community geography. Some of the more common ways for calculation include:

- Application of a uniform rate across the whole community regardless of land use (Uniform Development Charge).
- Application of a different levy rate for each type of land use (Land Use Specific Charges).
- Application of a variable rate for different areas of the community based upon well defined service areas (Sector Based Charges).

As these charges are often subject to significant scrutiny, choosing an approach which can be most easily defended is also a consideration that should be made. Industry best practices taken from other jurisdictions suggest that in most cases a Uniform Development Charge is favoured over a Sector Based Charge that applies a variable rate within a community. A Land Use Specific Charge provides a uniform application across a community but a variable rate is applied to residential and non-residential uses to represent their variable demand for and impact on municipal infrastructure.

We are recommending that a Uniform Development Charge be applied to all land uses within the community to minimize the complexity of managing the charge rates over time.

Where Wadena deems a capital infrastructure project to be specific to an area within the Town, they may consider adopting a Sector Based Charge for that area.

4 Program Time Frame

Development charges are based upon the forecasted servicing requirements for an anticipated amount of development that may occur over a certain period. Development charges can be established on either a build-out or a revolving basis.

A build-out approach includes all projects which will need to be constructed to realize the full amount of development anticipated by the current official community plan (OCP) which generally encompasses a 25-year time frame. Alternatively, a revolving approach identifies only projects that are necessary to facilitate growth over a specific time frame; aligning with the community's five-year capital planning process.

Utilizing a build-out approach promotes greater stability in rates over time but is often less accurate in assessing project costs given the propensity for economic changes to affect materials and labour rates over time. A revolving program is generally more defendable and based upon a documented commitment where aligned with the Town's capital budgeting process. Establishing a rate based upon a revolving approach aligns with the OCP but requires some further consideration by the Town in identifying priority growth areas and necessitates a greater commitment to promoting growth in these areas.

We are recommending that a build-out approach be taken to define the capital projects that comprise the development charge to minimize the complexity of managing the charge rates over time.

5 Unit for Charges

Development charges can be applied to development or subdivision on a site, building area, or per lot basis. The choice of which method to use comes down to administrative capacity and community characteristics.

Residential development charges are most typically applied on a per lot basis for single detached dwellings and a per dwelling unit basis for multi-family dwellings. These are considered the most appropriate units for assessment as they can be directly related to the population forecasts. Some jurisdictions assign the charge based upon a building's square footage which provides the most accurate estimation of its demand for services based upon the premise that a larger building will have a greater occupancy than a smaller building and as such will have a greater impact on municipal infrastructure. The problem with this approach is that it requires the application of the charge at the time of building construction whereas residential charges are generally charged at the time of subdivision. Another approach is to calculate the charge based upon the size of a lot or area basis. This encourages compact development by influencing the developer's decision regarding the number of units in an area recognizing that a smaller lot size reduces the per unit equivalent development charge cost. It is noted that it is common for lot area to be used to calculate commercial and industrial charges.

We are recommending that an area based unit is used for calculating both residential and non-residential development charges.

Where Wadena deems a capital infrastructure project to be specific to an area within the Town, they may consider utilizing a lot based charge.

6 Allocation for Benefit

At the foundation of financing growth is the principle that those that benefit from investments into new infrastructure should be held responsible for the cost of its construction and that growth should not come at the expense of the existing community. In determining the benefiting party, it is appropriate to ask the following question:

If no additional development were to occur, would this infrastructure project be required?

If the answer to the question is no, then it will be reasonable to allocate all or most of the financial responsibility to new developments which derive benefit from the new infrastructure. If the answer is yes, then it is assumed that the capital project benefits both existing and new development. Situations in which there might be a shared benefit includes:

- The repair or unexpanded replacement of existing assets;
- Maintaining or increasing the overall average service level or existing operational efficiency;
- Eliminating a chronic servicing problem not primarily created by growth;
- Providing services where none previously existed;
- Altering a service requirement primarily due to the change in needs of the existing population base; and
- Altering a service requirement primarily due to changes in regulatory requirements.

7 Development Charge Implementation

The following sections provide information relating to the implementation of development charges.

7.1 DEVELOPMENT CHARGE ADJUSTMENTS

Communities are often successful in receiving grants or other forms of financial assistance (i.e. federal/provincial funding, fundraising, private donor contributions, etc…) to offset growth-related capital costs. It is appropriate that the gross servicing costs be reduced by the anticipated value of third party grants and contributions to the extent that they are capable of being used to fund growth-related costs. This is generally acknowledged because the grants and other contributions are offsetting municipal costs of service, of which the benefits ultimately accrue to all system users. Where conditional grants have been secured by the Town towards a specific project, the project cost should be reduced by the amount of the grant. Unconditional grants, even though they may have been utilized by the Town for financing a project, are not deducted from the final project costs, as it can be rationalized that such funding could have been used for other projects.

We are recommending that any grants or alternative forms of funding received for the capital projects will be applied to reduce the gross project cost thus sharing the benefit proportionately between new and existing developments.

7.2 DEVELOPMENT CHARGE ASSESSMENT

We recommend that 50% of the total calculated development charges becomes due immediately upon execution of the servicing or development agreement and that the balance of development charges will be assessed incrementally as the serviced properties are sold and prior to the issuance of development and/or building permits. Net development area definitions will be applied in determining development charge obligations.

Net Developable Area (NDA) is defined as follows:

- **Gross Area –** The area of lands to be developed in hectares that have not previously been subject to a development charge.
- Less: Any environmental reserves contained within the development area including environmental reserves and environmental easements.
- Less: Allowance for Municipal Reserves.
- Less: Lands dedicated for public roadways.
- Equals: Net Developable Area.

The NDA is the area subject to development charges. Sections 171(3) and 172 (4) of the Act prohibit the assessment of more than one charge per development, or the assessment of a servicing agreement fee for work previously addressed by a development levy unless it can be demonstrated that the municipality will incur additional capital costs resulting from the proposed subdivision or development. The consequences of this is that where a subdivision of a new parcel occurs and a servicing agreement is executed to assess a servicing agreement fee for the subdivision, a development levy may not be assessed in the future on that property for any works previously undertaken or funded by the original servicing agreement fee unless it can be shown that the intensification of the property development will result in the municipality incurring additional capital costs as a result of the intensification.

7.3 DEVELOPMENT CHARGE CREDITS AND EXEMPTIONS

Development charges will not be collected on lands where:

- It can be shown or it is reasonable to assume that the land was previously connected to all municipal services including water, sanitary sewer, and storm drainage services and road access; or
- There will be a reasonable opportunity to collect offsite levies in the future, upon subdivision and further servicing of the land; or
- The land remains completely un-serviced.

Where a new service is provided to an existing residence but it is not appropriate to assess a charge in its entirety then an appropriate connection charge will be assessed to allow the service connection. The connection charge will be valued based upon the equivalent value of the development charge for that component only.

This occurs only where an existing, formerly un-serviced residence is connected to Town services where no planning, subdivision or zoning changes are contemplated. The Town may also consider providing a partial or full exemption where it is consistent with an adopted economic development initiative as a means of further encouraging the establishment of a specific type of new development, or density of development in strategic areas of the Town. Such an exemption would be funded within the broader tax structure.

Situations may arise where the timing for development precedes the timing for construction of the external infrastructure required to support the proposed development. The disconnection of timing creates a divergence between the Town's project budgeting and development charge fee funding.

We are recommending that the Town consider adopting a policy requiring a developer to be solely responsible for funding all external capital works which would have otherwise been provided by the Town where a development precedes its forecasted servicing. This private expenditure would be considered a loan to the Town to be credited against the calculated development charge with the outstanding balance repaid by the Town at a time in the future when the capital work was original intended to be completed based upon the Town's capital project schedule. This process allows for development to be front-ended by a developer who is then later reimbursed for their investment into external infrastructure works.

7.4 MUNICIPAL FINANCING, BUDGETING AND INFLATION

There is likely to be an occasional disconnection between the timing of capital infrastructure projects and development charge accounting, creating temporary funding shortfalls within the dedicated development charge account. This results in the potential need for the Town to provide temporary financing for these projects. A detailed financial plan forecasting and reconciling these anticipated divergences should be undertaken as part of the Town's regular five-year capital works budgeting process.

Recognizing that this is a living document and that economics change over time, it is essential that the cost estimates used to calculate the development charges be updated regularly to reflect annual inflation. It is also important to update these estimates as formal project tenders are received to ensure that the most accurate data is employed. The levy rate calculations should be fully updated at least once every five-years to match the Town's capital works budgeting cycle.