Report to Council

Department:	Office of the CAO
Division:	Legal and Legislative Services
Date:	April 6, 2021
Prepared by:	Robert Auger, Town Solicitor, Legal and Legislative Services/Clerk
Report Number:	Legal and Legislative Services-2021-06
Subject:	Front End Financing for Municipal Capital Facilities and a Policy for Future Large Scale Developments
Number of Pages:	18

Recommendation(s)

That Legal and Legislative Services-2021-06 entitled Front End Financing for Municipal Capital Facilities and a Policy for Future Large Scale Developments be received,

That Council approves the Town of Essex entering into an Agreement with Essex Town Centre Ltd. for the provision of municipal capital facilities in accordance with the terms and conditions of the said Agreement attached hereto as Schedule “A” to this Report;

That By-Law 1937 being a by-law to enter into an Agreement between Essex Town Centre Ltd. and the Town of Essex for the Provision of Municipal Capital Facilities be read a first, second and third time and be finally adopted on April 6 2021 ; and

That in accordance with this Report and its Agreement that Council direct Administration to formulate a formal policy to serve or guide future requests for assistance in relation to large scale developments in the Town of Essex.

Purpose

To approve the entering into of an Agreement for The Provision of Municipal Capital Facilities as it relates to the Essex Town Centre Subdivision Development (the 'Development").

Background and Discussion

At the June 15, 2020 Regular Council meeting Chief Administrative Officer Chris Nepszy spoke to Council about exploring options to develop a toolbox to encourage large scale development in the Town of Essex. At that June 15 meeting Council provided the following direction to continue with this review of options that could lead to the formation of a policy or policies to potentially guide future large scale development applications:

> **R20-06-201**
> Moved By Councillor Bowman
> Seconded By Councillor Garon
>
> **That** Council authorizes the Chief Administrative Officer to proceed with discussions and reviewing options on developing a policy that could provide assistance for large scale development projects in the municipality.
>
> **Carried**

While the development of a toolbox or a policy to encourage or promote development in the Town of Essex continues and will continue to be an evolving process, one of options that has been reviewed and is currently being proposed for the Essex Town Centre Development is an **"Agreement for the Provision of Municipal Capital Facilities"**. This proposed Agreement provides assistance, for a qualifying developer, in the way of "Front End Financing" by the Town, relating to the significant upfront costs required by a developer in connection with the Developer's construction of infrastructure for areas not currently serviced.

This proposed Agreement could serve the basis of what will hopefully:

1. Provide for a consistent approach for assisting qualifying developers, including establishment of the appropriate cost sharing structure between the development industry and the municipality, as well as for ensuring cost recovery.
2. Identify an acceptable level of risk to ensure that Town ratepayers are not unreasonably negatively impacted in terms of future tax or rate increases.
3. Develop an easy to follow decision making matrix, including criteria that can be

incorporated into the review of future Town of Essex development applications where front end financing of services is being considered; and

4. If adopted in principle, apply this approach to the Essex Town Centre Development as a pilot initiative and, if necessary, recommend ongoing amendments to the policies.

Generally, the Town is seeking to facilitate residential development of residential as part of its strategic objective for promoting economic development and growth. At the outset, it is observed that the servicing of undeveloped land is expensive and the Town needs to ensure that it only invests in developing those lands which will provide the Town with the best overall return on investment. In certain instances, it may not be in the Town's best interest to finance the servicing of lands and alternatively, there will be times where the Town should invest in servicing the lands. As part of this undertaking, an analysis of cost sharing and cost recovery methodologies should consider a range of options ranging from the status quo whereby the local services to be constructed by the developer remain 100% upfront financed by the developer to full front end financing whereby there is 100% upfront financing by the Town with future cost recovery from the benefitting lands.

Why Front End Financing?

There may be times where a developing landowner may reasonably request that a municipality consider assisting in accelerating the construction of the local services for a particular development.

The reasons for such a request from a Developer could vary widely but may include such reasons as:

- general cash flow timing issues for the development
- a large portion of the local services for the entire development need to be in place during the very early stages.
- the distance of how far the servicing needs to be extended and the cost involved in constructing this work, makes it unviable to undertake the project
- the need to oversize works or undertake other concurrent works

However the need for front end financing can also occur when it is desired or deemed necessary that a potential development proceed at a faster pace. From the Town's perspective it may be in its best interests to facilitate for such reasons as:

- an accelerated need for services based on market supply and demand.
- the development and its acceleration has a compelling advantage to the Town and region with respect to meeting housing and employment needs and growth targets
- the municipality may have challenges, unique or otherwise in attracting new development
- It is a significant sized development with expected population growth that may facilitate the development of other commercial development (and job creation or lead to the creation of other major facilities that are needed by the local community (i.e. a new school or a recreation complex)

With respect to the infrastructure required for a development, both the municipality and the developer generally share in the costs. The municipal cost is generally funded by development charges whereas the developer pays directly for their portion of such internal developer costs ("local services"). Local Services are those infrastructure costs to be borne directly by the developing landowner that are defined pursuant to the terms of the applicable municipal policy (developed as part of Development charge background study) or pursuant to the subdivision agreement or such other agreements entered into with the Municipality.

In order to facilitate or expedite such a development a municipality could consider constructing or fronting these localized costs and recover those costs directly from the benefiting lands over time. This could be achieved in mainly two ways: via either a localized Development Charge ("DC") by-law or through the use of Part 12 of the Municipal Act to impose a capital charge directly on the benefiting lands.

DC By-law vs. Part 12 of the Municipal Act

In regards to front end financing, a municipality may undertake an area specific (localized) DC by-law to recover the direct local service costs for an area. The process to be followed is exactly the same as a regular DC process and specific rules can be developed pertaining to timing of payment, basis of the charge, exceptions, etc.

Part 12 of the *Municipal Act* is where municipalities draw their authority to impose a wide range of capital and operating fees and charges. Many municipalities for example use this section of the Act to impose capital charges for localized water and sewer services instead of using the traditional Local Improvement Regulation. Generally the benefits of using Part 12 include:

- broader forms of charges can be imposed;
- more flexibility to address specific issues within the calculations;
- provides for full-cost recovery;
- the charge cannot be appealed to the OMB.

Similar to local improvements, the capital charges can be imposed immediately or on a delayed benefit basis. As well, loans can be provided (similar to local improvements) with interest and repaid over a period of time.

Both methods discussed above would facilitate recovery of the capital costs invested to service the lands. However, the localized DC By-law may have a longer cost recovery period (as full recovery would only be when full development of the area occurs).

The use of the Section 12 Municipal Act capital charge can accelerate the timing of recovery and thereby would have the lesser financial risk as again the localized DC would require a full build out of the lands in order to achieve full cost recovery.

This is the recommended approach in regards to the Essex Town Centre Development which approach can again serve as the basis for future large scale development applications.

The Proposed Agreement with Essex Town Centre Development

In this instance a request for front end financing was made by the developer (landowner) of the large planned subdivision known as Essex Town Centre Development. The request was made due to the large up front costs anticipated as a result of the large distances the infrastructure needs to extend for this particular subdivision and be in place early as part of the first phase of development.

The request was to provide financing of up to 100% (or a stated maximum loan amount) relating to the costs to construct the infrastructure for the storm water management system.

As a result of the request for assistance with financing, Town administration conducted further research as part of its due diligence to determine feasibility and further held meetings with this developer and worked towards the proposed agreement that Council now has before it as attached hereto to this report.

In working towards this proposed Agreement Administration was satisfied as to the following:

- demonstration of the need for these services in the shorter term
- landowner commitment to timely development through submission of all planning applications and or other requirements;
- Landowner commitment to share in the financial risk of extending services;
- Landowner commitment to accelerating the development.
- a significant sized planned housing community of at least 500 single detached or an equivalent mix of housing units with a build out population that will generate the need for future commercial development and services.

Legislative Basis for the Proposed Agreement

The authority or legislative basis for this proposed agreement (and any future agreements that may be entered into with other qualifying developers) is as follows:

- Pursuant to **Section 110 of the *Municipal Act***, the Town can lend money for the purposes of front end financing the cost of capital works known as "Municipal Capital Facilities".
- Pursuant to **Part 12 of the *Municipal Act***, the Town can impose charges on the lands benefiting from the constructed capital works as security for the loan amounts.

Section 110 Agreements for municipal capital facilities

This section allows for various property tax and development charge exemptions *and other financial assistance* to be provided by a Municipality in respect of certain municipal capital facilities:

110 *(1) This section applies to an agreement entered into by a municipality for the provision of municipal capital facilities by any person, including another municipality, if the agreement provides for one or more of the following:*

1. Lease payments in foreign currencies as provided for in subsection (2).
2. Assistance as provided for in subsection (3).
3. Tax exemptions as provided for in subsection (6).
4. Development charges exemptions as provided for in subsection (7).

This section has been used by various municipalities to provide such exemptions and/or assistance in regards to a wide range of facilities to be used by the Town and/or those facilities for the general administration of the municipality such as water, sewer and drainage facilities; cultural, recreation and tourist facilities.

This section further includes agreements for, among other things, assistance by the municipality in relation to those municipal capital facilities as defined further in Subsection (3) of section 110 as follows:

110 (3) Assistance by Municipality

Despite section 106, a municipality may provide financial or other assistance at less than fair market value or at no cost to any person who has entered into an agreement to provide facilities under this section and such assistance may include,

(a) giving or lending money and charging interest;

(b) giving, lending, leasing or selling property;

(c) guaranteeing borrowing; and

(d) providing the services of employees of the municipality.

"Despite section 106 " is a reference to the Section 106 general prohibition against municipal bonusing. Section 106 states that *"…a municipality shall not assist directly or indirectly any manufacturing business or other industrial commercial enterprise through the granting of bonuses for that purpose"* which in subsection (2) of Section 106 includes the "*giving or lending of any property of the municipality including money".*

While the general prohibition against municipal bonusing has actually only received minimum judicial interpretation , that exercise is not required in this case because Section 110 (3) provides for an explicit exemption from the prohibition against municipal bonusing.

This section 110(3) exemption allows for the providing of assistance by the municipality as it relates to agreements for the provision of "Municipal Capital Facilities" which is defined further in *Ontario Regulation 603/96* to include facilities such as:

- Municipal roads, highways and bridges.
- Municipal local improvements and public utilities.
- Municipal facilities for the generation of electricity.
- Municipal facilities for water, sewers, sewage, drainage and flood control.

As a result, as long as the loan or assistance is being provided and used for the purposes of the provision or construction of those municipal capital facilities the Town has the legislative basis or authority to provide such assistance to a developer.

Part 12 of the *Municipal Act*

This part of the Act and specifically Section 391 authorizes a municipality via by-law to impose fees or charges on persons for services or activities provided or done by or on behalf of it. Specifically Section 391 (2) provides that "*a fee or charge imposed for capital costs related to services or activities may be imposed on persons not receiving an immediate benefit from the services or activities but who will receive a benefit at some later point in time".*

This part of the Act specifically envisions the imposition of charges to recover expenses incurred by the Municipality and further allows for the immediate imposition of such charge notwithstanding the benefit to be received is deferred as would be the case in a situation where for example the Town has provided front-end financing to a developer for infrastructure/capital facilities still to be built/utilized.

The key is section 398 of the Act which provides that any such fees and charges imposed by municipal by-law shall become a debt of that person and may be added to the tax roll in respect of that property and collected in the same manner as municipal taxes.

Part 12 of the Act is critical then as it gives the Town security for the debt that may be outstanding if assistance is provided to a developer who then does not re-pay the debt in accordance with the terms of the Agreement. This charge will run with and remain upon the lands and this allows the Town to ultimately recover the cost of those capital facilities constructed by the developer but financed up front by the Town. Again this would only take effect in a situation whereby the developer has defaulted in respect of their repayment obligation but again it provides the Town security from a risk management perspective.

Details of the Proposed Agreement with Essex Town Centre Ltd.

The proposed agreement again was a result of the research and negotiations that ensued but the basic framework of this proposed Agreement could serve as a basic foundation or guide for future such agreements keeping in mind always that any future such agreements might need to adapt further to the scenario and facts presented.

An overview of the agreement (attached hereto as Schedule A to this report) and its main clauses are summarized below:

- **Recitals (I-IX)**– acknowledges the Town and Developer (Owner) are parties to the agreement, establishes the authority for the loan and for the recovery of the front ended funds;
- **Clause 2** – provides the statutory basis for the loan (Section 110 of the Municipal Act);
- **Clause 3** – acknowledges the list of capital facilities to be constructed with the loan proceeds (see Schedule C to the agreement) and that all works must commence within 18 months of agreement signing;
- **Clause 4 – provides for the details of the loan:**
  - Loan to be for the lesser of the actual costs of the Municipal Capital facilities or the maximum loan amount of $3,500,000;
  - Term of loan is 10 years with the entire loan then outstanding to be payable in full on the day that is ten years from the date of first advance;
  - Interest rate to be 3.94% compounded quarterly;
  - Any loan overages are to be borne by the landowner. Loan will not in any event exceed the maximum loan amount;
  - Payments on the loan will be on a quarterly basis beginning 3 months after the first advance.
  - The “Quarterly Payment Amount” shall consist of the following:

The amount of $7,500 per residential dwelling that is completed and sold in respect of the Development for the applicable Quarterly Payment Period; with such Quarterly payment to be applied firstly to interest accrued during such Quarterly Payment Period and the balance thereof if any, towards repayment of the principal outstanding. However if any quarterly payment fails to pay at least the interest accrued and outstanding at such time then the Owner agrees to make such payment to cover the interest accrued and still outstanding as of the date of such quarterly payment.

- Owner shall have the right at any time to prepay in whole or in part the loan amount;

- Owner agrees that the loan amounts can only be used for the purpose of providing the capital facilities noted and for no other purposes.
- Construction of the facilities will begin within 12 months of execution of the agreement and be completed within a commercially reasonable time thereafter.
- Any default in payment will entitle the Town to immediately add the outstanding amounts to the tax roll for collection thereof.
- Town may also require payment of any outstanding amounts to be further secured through the Subdivision Agreement security.

  - **Clause 6** – provides authority for the Town to pass a by-law under Part 12 of the *Municipal Act* to impose capital charges upon the lands to recover the cost for capital facilities upon a default in repayment of the loan. The security for this capital charge will be a charge/mortgage against title on those lands comprising 8 of the 12 phases of the development. Phase One and 3 other phases will be identified as those phases for initial lot servicing and development for residential sale and those phases will not have a capital charge imposed so as to allow the Developer to finance the ongoing residential housing works on those initial phases.

- The amount of the capital charge will be up to the maximum amount of $3,500,000.00 but such amounts and the corresponding security on those lands will be reduced proportionately as each of the twelve phases is completed provided there has been a corresponding pay down on the outstanding principal loan amount.
- **Clause 7** – Acknowledgment that any sale of the lands will require the purchaser of the land to be advised of the agreement;
- **Clauses 8 and 9** – provision for communication between the landowner and Town;
- **Clauses 10 to 18** – various caveats surrounding the agreement. Note that Clause 18 requires the payment by the developer/Owner of legal fees relating to the costs of this agreement and its ongoing administration;

There are expected to be three schedules to the agreement:

- **Schedule A** – applicable Subdivision Agreement
- **Schedule B** – Phasing Plan
- **Schedule C**- listing of municipal capital facilities to be built with loan proceeds:
    - Removal of existing watermain at Storm Water Management Pond;
    - Storm Sewer Construction, including installation of storm sewer drainage pipe and manholes;
    - Watermain Construction, including connections to existing mains, temporary backflow preventor and testing;
    - Storm Water Management Facility Construction, including excavation and grading of phase 1 interim pond;
    - Pump Station Construction, including pumps, piping, meters, valves and appurtenances, power supply and site work (including access road and driveway);

- Street Construction;
- Rush Drain Relocation;
- Noise Reduction Barrier Fence; and
- Engineering supervision.

- **Schedule D** – loan Repayment schedule to established upon first advance and updated on a going forward basis thereafter.

Overall Administration is hopeful that this agreement will in fact accelerate the development of what is truly a significant residential subdivision for the Town of Essex which could have lasting impacts on the future growth of the community.

The structure of the front end financing is specifically tied to the progress of the subdivision and provides an incentive for the developer to accelerate the building and sale of the residential homes as each residential home will contribute towards paying down the financing and associated interest charges.

The security on the loan (and its reduction thereof) is also tied to the progress of the subdivision and so again the developer has incentive to ensure the development progresses expeditiously. With a ten (10) year deadline for re-payment of the entire outstanding financing amount (with accrued interest), the Town also has an expected timeline for both the subdivision and the re-payment for the front-end financing that Is both defined and accelerated .

That is not to say that there is zero risk with this proposed agreement. While there is an element of risk to every venture not developing as planned, Administration feels that the risk associated with the front-end financing in this proposed agreement is at a minimum or acceptable level of risk to the Town giving the potential benefits to the Town that could be realized by this large scale residential development.

<u>Establishing a framework for a Large Scale Development Front End Financing Policy</u>

Suggested Criteria/Guidelines for Future Applications for Assistance.

While this proposed agreement and the analysis here will be restricted to residential developments

The key for future opportunities should be a “complete application” (under the Planning Act) submitted, along with the appropriate fees, supported by the following:

a) Demonstration of the need for the local services/capital facilities in the short term together with a compelling case as to why the particular developer is seeking assistance;

b) Demonstrated commitment to timely development through submission of all planning studies and applications;

c) Landowner commitment to share the financial risk of extending services.

Based on the above and the submitted documentation, an evaluation of the proposed development should be undertaken as follows:

Economic Development Evaluation

1. Review of projected growth forecasts;
2. Consider existing applications and market supply of land in general area;
3. Does the development application present a compelling case to the Town withrespect to meeting housing and employment needs and growth targets;
4. Is this is a significantly sized housing community with a build-out population that would generate a need for additional commercial development and hence wouldprovide some job creation (other than construction of infrastructure to facilitate the development) so that it makes accelerating longer term capital works desirable.

Infrastructure Evaluation

1. Availability of existing municipal servicing, and what is the range and extent of accelerated servicing required?
2. Is servicing capacity available for water and wastewater?
3. Consider logical progression of development to contiguous areas of the community – i.e. the development proposal does not constitute a "leap frog"development but is tied to a logical progression of the community;
4. An engineering evaluation to be undertaken to examine the technical feasibility of extending services to the area;
5. An engineering evaluation to analyze the capital improvements that may be required to facilitate additional flows or demands, including oversizing.

Development Evaluation

1. The benefiting area to be defined, including allocations of the benefit if there are multiple affected property owners;
2. An evaluation of the likely or necessary phasing or staging of services from an engineering and development perspective;
3. An evaluation of the likely timeline to achieve "build-out" of the lands by phase;
4. An assessment of the costs of providing services for each phase;
5. An evaluation of the timeline for the municipality to achieve "financial payback" of its investment costs through the assessment generated from new development;
6. Consideration of whether the Town's front-end financing of a particular development creates an unfair competitive advantage.

Assessment of Risk

Clearly, both the developing landowners as well as the Town seek to manage their risk. From the Town's perspective, risk assessment would consider:

- how much upfront cost is needed to undertake the project;
- how quickly can the costs be recovered
- impact on debt capacity for funding the capital costs.
- Security available and/or required to secure any financial assistance

Recommended Future Policy Approach for Front-End Financing:

It is recommended that front-end financing assistance for capital facilities should only be considered based on the following circumstances or criteria:

- **Large Scale Residential Developments** –large-scale master-planned "communities" of no less than 500 single detached units or equivalent thereof;
- **Scale** – relatively rapid staging of development providing a minimum of 50-100 units per year to be constructed;
- **Eligible Servicing Cost** – the local servicing cost to be front-ended must immediately benefit a minimum of 33-50% of the developable lands i.e. 33-50% of the developable lands benefitingfrom the servicing should be developable immediately or in the near future;
- **Level of front-end assistance** – Town should ideally target to cost share on a 50/50 basis but look to provide up to 100% up front assistance in certain circumstances where and when advisable;
- **Financing Terms:**
    - Competitive or close to competitive interest rate and repayment parameters;
    - Repayment term – 10 years from date of loan or less so as to encourage steady and/or rapid development;
    - The Town's overall debt capacity limit allocated to this Policy shall be capped at 50% of the balance in the Town's landfill reserve account.

While all of these recommended guidelines are being presented for Councils consideration , administration with Council support would continue to review and assess further (including the Essex Town Centre pilot initiative) as part of formulating an evolving policy relating to the front-end financing of a qualifying large scale residential development.

Financial Impact

This front end financing agreement policy could potentially lock up 50% of the Towns' landfill reserve for a period of up to 10 years from the point of disbursement. This amount is recoverable in full and will have priority lien status against the property in case of default. The amounts loaned under this policy will also form part of the Town's balanced investment portfolio with the interest earned being deposited directly into the Town's landfill reserve and thus growing the reserve.

Consultations

Chris Nepszy, Chief Administrative Officer

Jeffrey Morrison, Director of Corporate Services and Treasurer

Kevin Girard, Director of Infrastructure Services

Link to Strategic Priorities

☒ Manage, invest and plan for sustainable municipal infrastructure which meets current and future needs of the municipality and its citizens.

☐ Create a safe, friendly and inclusive community which encourages healthy, active living for people of all ages and abilities.

☐ Provide a fiscal stewardship and value for tax dollars to ensure long-term financial health to the municipality.

☐ Manage responsible and viable growth while preserving and enhancing the unique rural and small town character of the community.

☐ Improve the experiences of individuals, as both citizens and customers, in their interactions with the Town of Essex.

☐ Improve the Town's capacity to meet the ongoing and future service needs of its citizens while ensuring the corporation is resilient in the face of unanticipated changes or disruptions.