CITY OF HAMILTON

CORPORATE SERVICES DEPARTMENT

Financial Planning, Administration and Policy Division

TO:	Chair and Members Audit, Finance and Administration Committee
COMMITTEE DATE:	May 7, 2018
SUBJECT/REPORT NO:	City of Hamilton Development Charges By-law 14-153 Background Study Re: Industrial Development Expansion Policy Amendment (FCS18053) (City Wide) (Outstanding Business List Item)
WARD(S) AFFECTED:	City Wide
PREPARED BY:	Joe Spiler (905) 546-2424 Ext. 4519
SUBMITTED BY: **SIGNATURE:**	Mike Zegarac General Manager Finance and Corporate Services

RECOMMENDATIONS

(a) That Report FCS18053 be recognized as a DC Background Study under Section 10 of the *Development Charges Act, 1997, as amended,* for the purpose of providing background for amending definitions and policy of the existing Development Charge By-law 14-153;

(b) That the approval of Report FCS18053 be considered the Public Release of the DC Background Study as required by Section 10 (4) of the *Development Charges Act, 1997, as amended*;

(c) That the July 11, 2018 Audit, Finance and Administration Committee meeting be designated a public meeting as required under Section 12 (1) (a) of the *Development Charges Act, 1997, as amended*;

(d) That the City Clerk be directed to provide appropriate notice of the Public Meeting in accordance with Section 12 (1) (b) of the *Development Charges Act, 1997, as amended*;

(e) That Staff be directed to prepare an amending by-law for consideration following any and all public delegations at the July 11, 2018 Public meeting;

(f) That the impact resulting from an approved policy change related to industrial expansions be added to the 2019 Tax and Rate Budgets;

(g) That the matter respecting "Treatment of development charges with respect to industrial expansions" be identified as complete and removed from the Audit, Finance and Administration Committee Outstanding Business List.

EXECUTIVE SUMMARY

City of Hamilton Development Charges (DC) By-law 14-153 came into effect on July 6, 2014. By motion on March 28, 2018, Council directed:

> "That as part of the 2019 Development Charges By-law review, Finance staff, with support and assistance from Economic Development staff, research best practices and report back through the Development Charges By-law Review Stakeholder Committee, on options for competitive industrial Development Charges; and,
>
> That Finance staff, with support and assistance from Economic Development staff, review the practices of other municipalities specifically with respect to the treatment of expansions to existing industrial uses, and report back to the May 7, 2018 Audit, Finance & Administration Committee on potential amendments to the Development Charges By-law that could be put in place as an interim measure, pending the 2019 comprehensive Development Charges By-law review."

Staff examined various studies to determine the impact of DCs on a company's decision to expand operations as well as how surrounding municipal DC By-laws treat industrial development expansions.

Sections 17 – 20 of the City's DC By-law 14-153, which is attached as Appendix "B" to Report FCS18053, contain the following prescribed treatment for industrial development expansions:

> "Exemption for the Enlargement of Existing Industrial Buildings
>
> 17. No development charge shall be imposed on development constituting one or more enlargements of an existing industrial building as defined herein, whether attached or separate therefrom, up to a maximum of fifty percent (50%) of its gross floor area of the existing industrial building.
>
> 18. Where a proposed enlargement exceeds fifty percent (50%) of the gross floor area of an existing industrial building, development charges are payable on the amount by which the proposed enlargement exceeds fifty percent (50%) of the gross floor area before the enlargement.

19. The cumulative total of the gross floor area previously exempted hereunder shall not be included in the determination of the amount of the exemption applicable to any subsequent enlargement and shall be calculated on the basis of the site as it existed on the date immediately prior to the first exemption hereunder.

20. Where a subdivision of the site subsequent to any enlargement previously exempted hereunder results in the existing industrial building being on a lot separate from the development previously, further exemptions, if any, pertaining to the existing industrial building shall be calculated on the basis of the site as it existed on the date immediately prior to the first exemption hereunder."

At issue with the City of Hamilton's DC By-law 14-153 are Sections 19 and 20 (refer above), which limit the 50% industrial expansion DC exemption to the original building size and require consideration of any space previously exempted. Subsequent to the enactment of DC By-law 14-153, City staff released DC Interpretation Bulletin 1 which limits the frequency of eligible industrial development expansions to once every two DC By-law periods.

Staff's review and analysis of industrial policies revealed:

1. The majority of municipalities surrounding the City of Hamilton have fewer restrictions in their DC By-laws as it relates to industrial development expansions than the City of Hamilton.

2. Various studies and developer comments indicate that the relative amount of industrial property taxes and DCs do have an impact on where an industrial development locates and subsequent expansion plans.

3. Industrial development is a significant focus area in the City's Strategic Plan. Studies have shown that a municipality benefits from a healthy non-residential sector in terms of a City's overall assessment base. The more non-residential assessment that a City has, the healthier its fiscal outlook and one of the reasons for this is that an industrial development pays more in property taxes than it receives in direct services.

Subject to the recommendations contained in this Report, staff will bring a proposed amendment to the existing DC By-law to the July 11, 2018 Audit, Finance and Administration Committee meeting. Appendix "A" to Report FCS18053 provides a draft By-law amendment. The amendment removes limiting the exempted 50% expansion to the original building size and removes considering previous use of the 50% expansion exemption in the calculation of what can be exempted with each additional expansion.

This amendment is unable to be recommended today due to the legislative procedural requirements of the *Development Charges Act, 1997, as amended* ("Act").

A review of the industrial permit activity over the past two years indicates that the annual impact of the drafted policy change would have been approximately $500K annually. Considering the relevant split between tax supported and rate supported DCs, this increase would translate into a 0.03% municipal tax increase ($1 per average residential property valued at $337,100) and a 0.13% water, wastewater and storm rate increase. The impact of the policy change is recommended to be added to the 2019 Tax and Rate Budgets, estimated at $235K and $265K, respectively.

Note that Education DCs are levied by the School Boards and the City cannot impose policy on these. The current Education DCs are $0.39 per square foot for the Public Board and $0.34 per square foot for the Catholic Board. Since the City cannot impose policies on the Education DCs there is no further mention of them in this Report.

Alternatives for Consideration – See Pages 13-14

FINANCIAL – STAFFING – LEGAL IMPLICATIONS

Financial: The financial implications of the proposed changes will be dependent on the amount of industrial expansion that occurs. Any funds that are not collected through the DC By-law will need to be offset, either directly or indirectly, from another source (effectively, the property tax levy or water, wastewater and storm rates).

A review of the industrial permit activity over the past two years indicates that the annual impact of the drafted policy change would have been approximately $500 K annually. Considering the relevant split between tax supported and rate supported DCs, estimated at $235K and $265K, respectively, this increase would translate into a 0.03% tax levy increase ($1 per average residential property valued at $337,100) and a 0.13% water, wastewater and storm rate increase. The actual impact will vary depending on the amount of industrial activity and the success of the incentive in increasing the volume of industrial expansion activity.

Industrial Development Expansion Example

270,000 sq. ft. expansion
Original building = 100,000 sq. ft.
Expansion occurs in two 135,000 sq. ft. phases
Total DC amount with no exemptions at full DC Rate of $19.94 psf = $5,383,800
Total DC amount with existing exemptions = $2,675,200
Total DC amount with draft amendment exemptions = $1,246,400
Total DC exemptions under draft amendment = $4,137,400 or 77%

The increased property assessment would generate approximately $900K in additional municipal property taxes. This increase would translate to a payback period of approximately 4.6 years compared to the current 3.0 years to account for the additional foregone DC Revenues.

Additional financial and economic impacts include:

Total capital investment by developer - $40M

New employees expected with all phases completed:

- Direct positions 80 to 100 full-time

Spin off jobs, all phases:

- Design and co-ordination, 30 full-time positions
- Construction, 100 man-years
- Indirect spin-off jobs due to increased manufacturing capacity – 600 to 800 (includes suppliers, vendors, consultants, craft labour, supporting services, etc.)

The amount exempted would depend on the size and frequency of expansions. With each subsequent expansion, the amount that would be exempted would increase. If a developer were to always expand under the 50% limit, then they would not pay any DC.

Staffing: None

Legal: Report FCS18053 functions as the background study required by the *Act* to be released at a minimum of 60 days prior to the passing of any new or amended DC by-law. In order to amend a DC By-law there are other legal responsibilities such as holding a public meeting and providing notice of said public meeting.

HISTORICAL BACKGROUND

DC By-law 14-153 came into effect on July 6, 2014. As per the *Act*, DC By-laws can be in effect for a maximum period of five years before a new background study and By-law are required to be enacted. However, municipalities may elect to enact a new By-law or amend their By-laws before the five-year period expires.

By motion on March 28, 2018, Council directed staff to review the policy as it relates to industrial development expansions and competitiveness with surrounding municipalities.

POLICY IMPLICATIONS AND LEGISLATED REQUIREMENTS

The *Act* requires a background study prior to passing a DC By-law. The current DC By-law came into force on July 6, 2014. A new DC By-law will be required to come into force on or before July 6, 2019. The work to undertake a complete City-wide DC background study and by-law utilizing the Province's original 2031 growth forecasts and exiting Infrastructure Master Plans has been initiated through Reports FCS17086 and FCS18034. There is no change or edit recommended to this process that would be impacted by a DC By-law amendment.

Report FCS18053 would function as a background study for the purpose of amending the existing wording contained within DC By-law 14-153. The background study is required to be public for a minimum of 60 days before Council may pass the amendments. There must also be at least one public meeting prior to passing the amendments. Staff, including staff of the City Clerk's division, will work to meet the legislative requirements and finance staff will bring a report to the July 11, 2018 Audit, Finance and Administration Committee meeting which could amend the existing DC By-law.

Section 19 of the *DC Act* requires that Sections 10 through 18 of the *DC Act* be applied for an amendment of an existing DC By-law. Section 10 requires a background study with some prescribed detail. The by-law amendments being considered, namely changes to definitions and policy, impact only the by-law and do not necessitate a change to the growth forecast, capital costs or calculation of the quantum as prepared by Watson & Associates Economists Ltd. through the detailed work in the 2014 DC Study. The full document can be accessed on the Development Charges Overview webpage on www.hamilton.ca.

Watson & Associates Economists Ltd. have reviewed potential amendments and have confirmed that Report FCS18053 meets the requirements of a background study. The confirmation from Watson & Associated Ltd. is included as Appendix "C" to this Report FCS18053.

To amend a DC By-law, a municipality must go through the same public process associated with enacting a DC By-law. A background study outlining the purpose of and rationale for the amendment is required. This document serves as the background study required under Section 10 of the *DC Act*. The background study only needs to consider the impact of the amendment.

Table 1
DC Act Requirements of What is to be Included in a Background Study

Section		Applicability to amendment
10 (1)	Before passing a development charge by-law, the council shall complete a development charge background study	Report FCS18053 is the background study.
10 (2)	The development charge background study shall include,	
	(a) the estimates under paragraph 1 of subsection 5 (1) of the anticipated amount, type and location of development;	The estimate of the anticipated amount, type and location of development considered in the original 2014 Development Charges Background Study which was used in the calculation of DC rates for the current DC By-law has not materially changed as a result of the amendment proposed. A full review and update will occur with the replacement by-law due to be in place prior to expiry of DC By-law 14-153.
	(b) the calculations under paragraphs 2 to 8 of subsection 5 (1) for each service to which the development charge by-law would relate;	The calculations under paragraphs 2 to 8 of subsection 5 (1) for each service to which the development charge by-law relates in the original 2014 Development Charges Background Study which was used in the calculation of DC rates for the current DC By-law has not materially changed as a result of the amendment proposed. A full review and update will occur with the replacement by-law due to be in place prior to expiry of DC By-law 14-153.
	(c) an examination, for each service to which the development charge by-law would relate, of the long term capital and operating costs for capital infrastructure required for the service;	The long term capital infrastructure and operating costs for capital infrastructure required for each service work performed in the original 2014 Development Charges Background Study which was used in the calculation of DC rates for the current DC By-law has not materially changed as a result of the amendment proposed. A full review and update will occur with the replacement by-law due to be in place prior to expiry of DC By-law 14-153.

	Section	Applicability to amendment
	(c.1) unless subsection 2 (9) or (11) applies, consideration of the use of more than one development charge by-law to reflect different needs for services in different areas;	While not a requirement when the original 2014 Development Charges Background Study was published, any work related to area specific charges would not be materially changed as a result of the amendment proposed. A full review and update will occur with the replacement by-law due to be in place prior to expiry of the current by-law.
	(c.2) an asset management plan prepared in accordance with subsection (3); and	While not a requirement when the original 2014 Development Charges Background Study was published, the impact any work related to asset management plans would not be materially changed as a result of the amendment proposed. This amendment does not involve the addition of any capital projects or changes to the cost of any capital projects included in the 2014 Development Charges Background Study. Further, it will not increase any operating costs for any new infrastructure to be funded, in part, from development charges. A full review and update will occur with the replacement by-law due to be in place prior to expiry of the current by-law.
	(d) such other information as may be prescribed	No other information has been prescribed to date

Table 2
Schedule of Dates for the DC By-law Amendment Process

Background Study and proposed by-law amendment available to public	May 7, 2018
Public Meeting ad placed in newspaper(s)	June 2018 At least 20 days prior to the public meeting
Public Meeting	July 11, 2018
Council considers passage of by-law	AF&A – July 11, 2018 Council – July 13, 2018 No less than 60 days after the background study is made available to the public
Newspaper and written notice given of by-law passage	By 20 days after passage
Last day for by-law appeal	40 days after passage
City makes available pamphlet (where by-law not appealed)	By 60 days after passage

RELEVANT CONSULTATION

Economic Development, Planning and Economic Development
Legal Services Division, Corporate Services Department
Watson & Associates Economists Ltd.

ANALYSIS AND RATIONALE FOR RECOMMENDATIONS

Staff examined various studies to determine the impact of DCs on a company's decision to expand operations as well as how surrounding municipal DC By-laws treated industrial development expansions.

Table 3
Municipal Industrial Comparison

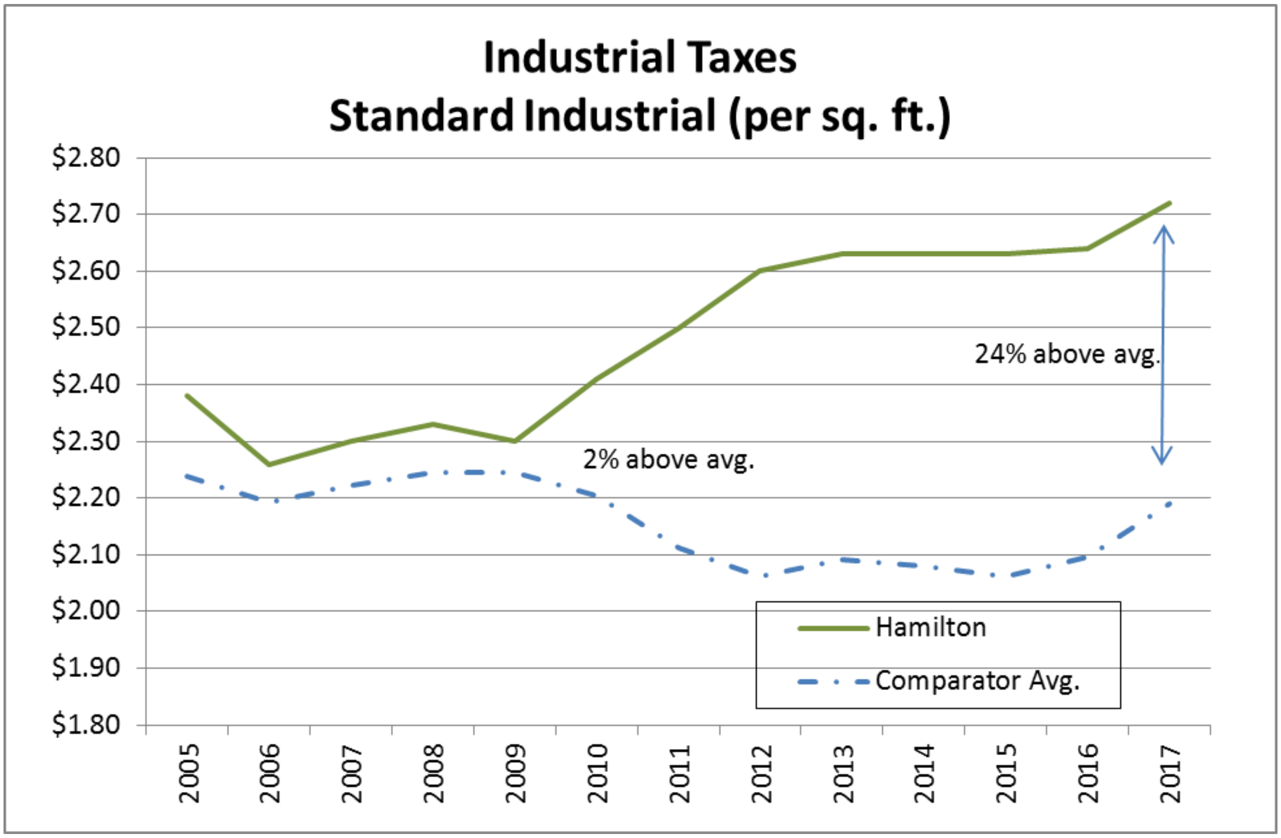
	2017 Total Industrial Tax Rates (inc. Education)	2017 Industrial DC Rate ($ per sq.ft.)	DC By-law Industrial Expansion Policy
Hamilton*	5.1811% / 5.8543%	12.16	Expansion doesn't have to be attached, two by-law periods must pass prior to next eligible expansion.
Halton Region	n/a	10.26	Expansion needs to be attached.
Burlington**	2.9600%	7.38 / 10.26	Expansion needs to be attached. Limited to original size. Once 1.0 lot coverage is achieved there are no further DCs assessed.
Milton**	2.6169%	3.23 / 10.26	Expansion needs to be attached. Limited to original size.
Niagara Region	n/a	4.43	Limited to original size. Grant Program available for offset.
Grimsby**	4.0716%	3.33 / 4.43	No restrictions.
West Lincoln**	4.0145%	2.95 / 4.43	No restrictions.
St. Catharines**	4.7690%	0 / 4.43	No restrictions.
Ottawa*	3.7947% / 3.4400%	8.84	No restrictions.
City of Waterloo**	3.2448%	6.36 / 5.69	Expansion needs to be attached. Limited to original size.
Guelph	3.6454%	9.68	Limited to original size.
London	3.6938%	0	No restrictions.
Brant County	n/a	6.48	Expansion needs to be attached. Limited to original size.
Brantford	4.2684%	6.3	No restrictions.
Woodstock	4.8547%	0	No restrictions.

* The two property tax rates reflect small industrial and large industrial rates.

** The two DC rates reflect the lower tier and upper tier (region) DC rates

Table 3 illustrates that when compared to surrounding municipalities, Hamilton has the highest industrial property tax rate and one of the higher industrial DC rates. In addition, the surrounding municipalities, especially to the west, have less restrictive industrial expansion policies imbedded in their DC By-laws.

Figure 1



Source: BMA Study 2017

In addition, staff has recently reported the results from BMA Tax Competitiveness Study 2017 in Report FCS18021 to the General Issues Committee. Figure 1 shows the gap between Hamilton and comparable municipalities in the Standard Industrial property class for sample properties under 125,000 sq. ft. in size. The gap has changed over time but now is around 24% above average.

There are several studies which indicate that taxes, such as the property tax and DCs, are significant factors in where an industrial development locates and / or expands. Like the property tax, DCs are a significant cost for industrial development. Professor Harry Kitchen (researcher of Canadian Taxation and Public Policy Issues), a presenter to the Hamilton Economic Summit in April 2018, wrote the following in a Property Taxes and Competeviness in British Columbia Report (May 2012):

> "Heavy taxation of the non-residential sector has been addressed in a few Canadian studies. All of these estimated the benefits that the non-residential sector gets from the consumption of local public services and compared this value to the property tax paid by the non-residential sector. All studies found that the residential sector receives proportionately more benefits from local government services than the non-residential sector. For example, the non-residential sector relies less heavily on social services, social housing elementary and secondary education, libraries, recreational facilities, and it is often responsible for providing its own garbage collection, security, and fire protection.
>
> A very important issue is whether the higher taxes on business properties plays a role in location decisions. Firms and businesses generally locate where they can maximize profits, so property taxes can influence a firm's location decision in the same way as any other cost of production. The impact on location decisions of property tax differentials depends on a number of factors including the size of the differential between competing municipalities and whether this differential is sufficient to offset differentials in other costs or market factors.
>
> There is no general agreement about the importance of property taxes in location decisions. The available evidence, most of which is drawn from the United States, suggests that property tax differentials are relatively unimportant in inter-municipal or inter-regional location decisions but do play a role in intra-municipal or intra-regional location decisions (Kitchen and Slack, 1993). In other words, differences in property taxes are unlikely to play a significant role in a firm's decision whether to locate in the metropolitan areas of Vancouver, Calgary, Montreal, Halifax or Toronto. They are likely to play a role, however, once a firm or business decides to locate in a certain region such as the Greater Toronto Area, Metro Vancouver or the Region around Montreal. Indeed, one might expect property tax differentials to produce a heavy concentration of all firms and businesses in the jurisdictions with the lowest effective tax rates. In other words, intra-municipal tax competition may be destructive if it leads to a race to have the lowest tax rates. "

Travis Allen and Cherise Burda of the Canadian Pembina Institute (a non-profit think-tank who work with various senior levels of government on policy issues) wrote the following in May of 2013 in their Article "Re-tooling development charges into a sharp, effective revenue tool":

> "Taxes and Fees paid by commercial properties in the City of Toronto are high compared to surrounding municipalities. This tax differential has been identified as a key factor in driving commercial development out of Toronto's transit-oriented core to surrounding municipalities that have even less transit service: the so-called "business park Badlands". If we increase commercial development charges across the board, we may contribute to this problem, driving even more commercial development out of the City of Toronto."

Also, CBRE Canada Research Team which forms part of CBRE Global Research and Consulting prepared the following "Greater Toronto Area Industrial Market Snapshot" for October 2013. It stated the following:

> "The GTA could see industrial DCs rise to some degree, if not the entire 15.0% that is proposed by Metrolinx, over the next five years. As a result, a wave of new industrial construction is expected in advance of a spike in DCs. There was a similar spike in development permit issuance and construction in the third quarter of 2012, prior to a scheduled hike in industrial DCs in Peel and Halton Region. In Mississauga, the number of industrial building permits nearly doubled between the third and fourth quarters of 2012. Unlike office construction, industrial development can be scaled up or down very quickly as project timelines are shorter.
>
> Currently, 80.0% of construction activity is located in the western portion of the GTA, primarily in Halton and Peel Region, with the remainder located in York Region. The western portion of the GTA will continue to attract industrial development due to its access to the 400-series highway network, rail lines, as well as the proximity to Toronto Pearson International Airport, Canada's busiest airport.
>
> Although DCs are not intended to be used as a tool to manage or direct growth and construction, they have that potential. Developers could choose to build outside of the GTA, undermining the government's potential to raise revenue from DCs, defeating the intended purpose of the rate hike.
>
> Even in this second scenario, developers concerned about rising DCs have options. All municipalities in the GTA have a by-law that allows developers to expand the industrial gross floor area for an existing building up by to 50.0% without paying DCs. Therefore increase total inventory without incurring additional DCs. For example, much of Orlando Corporation's new industrial space in Brampton has the potential for future expansion without significant DCs. Other notable developers such as HOOPP and First Gulf Corporation are taking this into consideration as they plan for the future of their industrial portfolio."

When City of Hamilton's staff asked a developer who had an existing industrial building in Hamilton but expanded in another municipality for the reasoning, he replied;

> "That the global land price (including DC's) and highway access were critical factors. You could add surrounding area around the industrial park (without housing, no wetland, easy access, services available). The future expansion of the site was also a top priority for us."

City staff further inquired with existing industrial businesses to assess how more flexibility regarding DCs on expansions would impact their future expansion plans. The following responses were received:

"We recently finished our expansion at 1430 Cormorant and we are already thinking of expanding in 2021 thereby increasing number of employees by 30%. If we were allowed to do this with the 50% saving in development fees, it would certainly make us more aggressive in our expansion plans." – Everest Wholesale

"As long time Business Owners and Industrial Real Estate Developers in the Ancaster Business Park, we took advantage of the development charge expansion credits to help our large Multi-National anchor tenants expand their businesses. We appreciate all efforts made by Hamilton Economic Development Division, as access to the DC program promotes development and brings employment opportunities to Hamilton." – Advanced Tenant Properties

"Thank you for reaching out to me on the matter of possible changes to the development charge by-law for the region. We find this form of taxation to be the most difficult to accept and absorb for the following reasons. Very few competitors in the USA have to pay this, in fact, if anything, they receive valuable incentives to attract companies such as Janco Steel. If we go through the massive decision and expense to expand, on top of all those costs, the development charges need to be paid right away and yet must be capitalized (expensed) over a 25 year term. If the city already gets added property business tax because of the extra square footage we are putting up, then this charge represents an onerous form of double taxation. Our last expansion (2017) was a 50,000 square foot building in the Elmira area where the taxes are lower and the building costs were more manageable. Enough said .... We had options and we exercised them. Any expansion in Hamilton will need to offer relief in these areas to help attract manufacturers, in my opinion. Although we are proud to be Canadian and love the community, we live in a global village that demands us to be competitive on a world scale. In the absence of progress in these areas of concern, we will have little choice but to expand elsewhere in the future. Hoping that the Council will give careful thought to your proposal for the wellbeing of the region." – Janco Steel

The preceding studies and the local developer's comment reinforce the fact that DCs are a significant industrial development cost and influential in locational decisions.

ALTERNATIVES FOR CONSIDERATION

Alternative 1: Refer Industrial Development Expansion Policy Amendment to the 2019 DC By-law Process

Alternatively, Council could not take any action at this time. Under this alternative, staff would utilize the background information contained within Report FCS18053 with the 2019 DC Background Study and any resulting change to the industrial policy would be determined at a later date.

Financial: The current industrial DC policies would be applied and DCs charged and collected according to those policies.

Staffing: None

Legal: None

Pros: Industrial DCs for expansion would be levied according to current policies.

Cons: Developers may make a decision to expand outside the City or delay expansion plans based on the DC levy.

Alternative 2: Revise Draft Industrial Development Expansion Policy DC By-law Amendment to Account for Previously Exempted Space

Under this alternative, an amendment to the DC By-law would still be sought similar to the drafted amendment attached as Appendix “A” to Report FCS18053 with the available 50% industrial expansion exemption being calculated based on total buildings on site but with the caveat that the available exemption be reduced by any previous exemptions the development has received.

Financial: Compared to the drafted DC By-law amendment, attached as Appendix “A” to Report FCS18053, this alternative would result in a higher amount of DCs being collected on industrial expansions.

Staffing: None

Legal: The same legal process applies to this recommendation as it does to the current recommendation.

Pros: More DC funds collected from industrial expansions.

Cons: May not provide the level of incentive needed to encourage industrial developments to expand in Hamilton versus outside the City.

ALIGNMENT TO THE 2016 – 2025 STRATEGIC PLAN

Community Engagement & Participation

Hamilton has an open, transparent and accessible approach to City government that engages with and empowers all citizens to be involved in their community.

Built Environment and Infrastructure
Hamilton is supported by state of the art infrastructure, transportation options, buildings and public spaces that create a dynamic City.

Our People and Performance
Hamiltonians have a high level of trust and confidence in their City government.

APPENDICES AND SCHEDULES ATTACHED

Appendix A – Draft Amendment for City DC By-law 14-153

Appendix B – DC By-law 14-153

Appendix C – Memo from Watson & Associates Economists Ltd.

JS/dt