



Hamilton

**CITY OF HAMILTON**

**CITY MANAGER'S OFFICE  
Audit Services Division**

<b>TO:</b> Chair and Members Audit, Finance and Administration Committee	<b>WARD(S) AFFECTED:</b> CITY WIDE
<b>COMMITTEE DATE:</b> April 6, 2011	
<b>SUBJECT/REPORT NO:</b> Audit Report 2010-10 - Development Charges (AUD11016) (City Wide)	
<b>SUBMITTED BY:</b> Ann Pekaruk Director, Audit Services City Manager's Office	<b>PREPARED BY:</b> Ann Pekaruk 905-546-2424 x4469
<b>SIGNATURE:</b>	

**RECOMMENDATION**

- (a) That Report AUD11016 respecting Audit Report 2010-10, Development Charges, be received;
- (b) That the management action plans as detailed in Appendix "A" of Report AUD11016 be approved; and,
- (c) That the General Managers of Planning and Economic Development and Finance and Corporate Services be directed to instruct the appropriate staff to have the Management Action Plans (attached as Appendix "A" to Report AUD11016) implemented.

**EXECUTIVE SUMMARY**

The 2010 Internal Audit work plan approved by Council included an audit to review the controls related to the implementation, recordkeeping, monitoring and effectiveness of development agreements. Financial aspects such as fees and cost recovery, legislative compliance, enforcement of development agreements and reserve funds activities were reviewed. Recommendations were made to strengthen processes and identify opportunities for administrative improvements.

The results of the audit are presented in a formal Audit Report (2010-10) containing observations, recommendations and management responses. In addition, an Addendum which identifies issues, risks or inefficiencies (not necessarily control deficiencies which appear in Report AUD11016) is included and management has been asked to address these points also. Audit Report 2010-10 and the Addendum are attached as Appendix "A" to Report AUD11016.

***Alternatives for Consideration – Not Applicable***

**FINANCIAL / STAFFING / LEGAL IMPLICATIONS** (for Recommendation(s) only)

**Financial:** None.

**Staffing:** None.

**Legal:** None.

**HISTORICAL BACKGROUND** (Chronology of events)

Development charges are meant to recover a portion of costs associated with the additional infrastructure needed to service new development. These revenues are an important source of funds used by the City to finance capital investments required for a growing urban area. In order to pass a development charges by-law, a background study to identify growth related projects and determine the charges to be imposed needs to be conducted. The City's most recent background study was completed in 2009 in which rates were set to recover the costs estimated to be incurred on capital projects identified in the study. However, Council deferred the charge rate increases for a period of one year until July 6, 2010. The rates are also indexed by the percentage change recorded in the Statistics Canada Construction Cost Index from the preceding year, annually on each by-law anniversary date.

The audit was scheduled as part of the 2010 Internal Audit work plan approved by Council. The audit fieldwork was completed in January, 2011. The results of this audit are attached as Appendix "A" of Report AUD11016.

The Audit, Finance and Administration Committee receives and approves final audit and review reports as part of its responsibilities for the oversight of governance and control.

**POLICY IMPLICATIONS**

- Development Charges Act, 1997, s.2
- City of Hamilton by-laws: 09-143, 09-144, and 06-174

### **RELEVANT CONSULTATION**

Appendix "A" to Report AUD11016 includes management action plans which reflect the responses of management and staff responsible for the implementation, recordkeeping and monitoring of development agreements and charges – Building Services Division, Planning and Economic Development Department and Financial Planning & Policy Division, Corporate Services Department.

### **ANALYSIS / RATIONALE FOR RECOMMENDATION**

(include Performance Measurement/Benchmarking Data, if applicable)

The purpose of development charges (DC) is to recover the growth related costs associated with the capital infrastructure needed to service new development. The Province enacted the Development Charges Act (the Act) in 1997 which granted municipalities the authority to develop by-laws to impose development charges. The City of Hamilton has three such by-laws: 09-143, 09-144, and 06-174. By-law 09-143 covers costs related to a variety of services such as roads, storm water, ambulance and police while By-law 09-144 is specific to the growth related costs of water and wastewater services. By-law 06-174 covers the increased growth related costs associated with GO Transit. In the 11 month period of January to November, 2011, over \$37 million in development charges was collected.

According to the Act, development charges are payable when a building permit is issued and the City's Development Charges by-laws are consistent with this requirement. Further, the City's DC by-laws allow for the deferral of DC for specific types of development and specific time periods. In order for DC to be deferred, a Deferral Agreement authorized by Council must be in place.

Development charges collected are allocated to appropriate reserve funds. At December 31, 2009, the total amount held in the City's various development charges reserve funds was \$35.1 million. During 2009, \$22.5 million in contributions and interest were added to the reserve funds and \$33.7 million was used for expenditures on eligible growth capital projects.

The audit set out to assess the management controls in place to ensure compliance with relevant legislation, policies and procedures when determining the amount of development charges payable. The effectiveness of administrative controls for monitoring and accounting for development funds received was also reviewed. In addition, procedures which ensure development fees are allocated to the appropriate reserve funds were examined.

A formal Audit Report (2010-10) containing observations, recommendations and resulting management action plans was issued. The implementation of the four (4) recommendations included in the Audit Report 2010-10 and Addendum (attached as Appendix "A" of Report AUD11016) will strengthen internal controls for collecting development charges, achieve processing efficiencies by automating manual business processes and improve the accountability for the administration and collection of development charges. The recommendations are as follows:

- Develop written procedures for the collection of development charges and allocation of fees to the reserve funds accounts.
- Implement Information Technology controls to safeguard the recorded date building permit applications are received.
- Investigate opportunities to streamline and automate processes to reduce the reliance on manual methods.
- Send reminder notices for deferred development charges 45-60 days in advance of due dates.

Staff have agreed with all the recommendations and their management action plans are included in Appendix "A" to Report AUD11016.

#### **ALTERNATIVES FOR CONSIDERATION**

(include Financial, Staffing, Legal and Policy Implications and pros and cons for each alternative)

Not applicable.

#### **CORPORATE STRATEGIC PLAN (Linkage to Desired End Results)**

Focus Areas: 1. Skilled, Innovative and Respectful Organization, 2. Financial Sustainability, 3. Intergovernmental Relationships, 4. Growing Our Economy, 5. Social Development, 6. Environmental Stewardship, 7. Healthy Community

#### ***Financial Sustainability***

- ◆ Delivery of municipal services and management of capital assets/liabilities in a sustainable, innovative and cost effective manner.
- ◆ Address infrastructure deficiencies and unfunded liabilities.
- ◆ Generate non-tax revenues.

#### **APPENDICES / SCHEDULES**

Appendix "A" to Report AUD11016: Audit Report 2010-10

ap:tk/dt

**CITY OF HAMILTON  
INTERNAL AUDIT REPORT 2010-10  
DEVELOPMENT CHARGES**

#	OBSERVATIONS OF EXISTING SYSTEM	RECOMMENDATION FOR STRENGTHENING SYSTEM	MANAGEMENT ACTION PLAN
1.	<p><u>Written Procedures</u> In 2010 (year-to-date November 30), over \$37 million was collected for development charges. Several divisions are involved in the process yet only Treasury Services, which prepares the bank deposit, has developed written formal procedures to guide staff in performing their duties.</p> <p>Without written procedures, the employees currently carrying out related processes rely on personal understanding and experience which may result in incorrect, incomplete or inconsistent application. Also, it may be problematic and inefficient for a successor to commence his/her duties within a short period of time.</p>	<p>That written procedures be developed for the collection of development charges in Building Services and the allocation of fees to the reserve accounts in Financial Planning and Policy.</p>	<p>Agreed. Finance staff will work with Building Services staff to complete a set of written formal procedures before the next Development Charge By-law anniversary date of July 6, 2011.</p>

**DEVELOPMENT CHARGES  
JANUARY 2011**

#	OBSERVATIONS OF EXISTING SYSTEM	RECOMMENDATION FOR STRENGTHENING SYSTEM	MANAGEMENT ACTION PLAN
2.	<p><u>Monitoring</u></p> <p>According to the development charges by-laws, the amounts payable are based on the rates in effect on the date a completed building permit application is received and accepted by the Customer Service Representative in the Building Services Division (provided a building permit is issued within six (6) months of the development charge rate increase). The development charges are due at the time the building permit is issued. Therefore, it is important that for each permit application, a record be maintained of the date that the building permit application is received (the "in date" in the AMANDA application) as well as the date that the building permit is issued (the "issue date" in AMANDA) in order to be able to ensure that the correct amount is charged for development fees. This would especially be true when there are large increases in the charges as of a certain date as there were on July 6, 2010 when some fees increased over 30%.</p> <p>Staff in Building Services have the ability to change the "in date" and "issue date". Therefore, this makes it difficult to readily determine whether the correct development fee was collected from the developer.</p>	<p>That the two dates that are required to ascertain that the correct development fees are being charged be protected from being changed once they have been input into the AMANDA system.</p>	<p>Agreed. Finance will work with Building Services and IT to see if this recommendation is feasible. Target date: 4th quarter 2011.</p>

**DEVELOPMENT CHARGES  
JANUARY 2011**

#	OBSERVATIONS OF EXISTING SYSTEM	RECOMMENDATION FOR STRENGTHENING SYSTEM	MANAGEMENT ACTION PLAN
3.	<p><u>Allocation of Fees</u></p> <p>Monthly development charges collected are allocated to the various reserve accounts according to the weighting determined by the Background Study conducted by independent consultants. The development charge information is gathered from paper documents related to the building permit and is manually entered into a spreadsheet. The data must be sorted by several different criteria and the results compared to those in the PeopleSoft financial system. The sorted information is entered into another spreadsheet in order to allocate the amounts to individual development charges reserves.</p> <p>This method is labour intensive, involves manual input and duplicates entry in different electronic spreadsheets. Due to the number of steps involved and the lack of automation, it is easy for an error to occur and remain undetected.</p>	<p>That Financial Planning and Policy investigate alternate means to streamline and automate the allocation process to reduce the reliance on manual methods.</p>	<p>Agreed. Staff will work with IT to determine the degree of additional automation feasible. Target date: 4<sup>th</sup> quarter 2011.</p>

**CITY OF HAMILTON  
INTERNAL AUDIT REPORT 2010-10  
DEVELOPMENT CHARGES**

**ADDENDUM**

The following items were noted during the course of the audit. Although they do not present internal control deficiencies, they are indicated in this Addendum so management is aware of the issues, risks and inefficiencies and can address them appropriately.

Deferred Development Charges Agreements

1. The City of Hamilton's Development Charges by-laws allow the City to enter into agreements with individuals for deferring development charges on non-residential developments (including apartment buildings) for up to five years but may require the repayment to include interest. In the course of this review, it was noted that 20 such agreements with deferrals ranging from \$20,000 to \$2.5 million are currently open. In a situation noted during the audit, the holder of one such deferred development charges agreement that had come due was not reminded of the payment until the day before it was due. This necessitated a request to Council to change the repayment terms, affecting the flow of funds due to the City.

***It is recommended:***

***That the Development Financial Officer be assigned the responsibility of reviewing the due dates of the deferred development charges agreements monthly for the purpose of notifying Accounts Receivable to send notification of amounts due to the developer 45-60 days in advance.***

***Management Response:***

***Agreed. In addition to the actions recommended above, Finance staff will look at additional trigger points (i.e., from A/R) so that this oversight cannot happen again. This will be implemented immediately.***