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**OBTAINING AMENITY CONTRIBUTIONS  
FROM NEW URBAN DEVELOPMENT PROJECTS:  
DISCUSSION PAPER FOR THE CITY OF VICTORIA, BC**

**DRAFT**

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## 1.0 Introduction

The City of Victoria is creating an updated Downtown Plan that is intended to help achieve a lively, mixed use core that is both an attractive, high density residential neighbourhood and a strong contributor to the local economy as a regional retail centre, regional business/government centre, and tourism destination.

To achieve this vision, the City wants to expand the tools it has available to protect the large stock of Downtown heritage buildings and to secure amenities that will enhance Downtown's appeal as a high density housing and employment centre. The City is particularly interested in refining its approach to obtaining amenity contributions from new urban development projects in Downtown, to help make Downtown more attractive to residents and businesses.

The City can use Development Cost Charges to generate funds for basic infrastructure that serves growth, but not for other important community amenities such as recreational facilities or fire halls. To help achieve the City's social, economic, and environmental goals in Downtown, Victoria currently makes limited use of density bonuses on a case-by-case basis to obtain some amenities. However, the City is exploring ways in which it could obtain more amenity contributions from new development to enhance Downtown and defray the costs of growth.

As part of the new Downtown Plan, the City wants to adopt an approach to amenity contributions that is well thought out, consistently applied, fair-minded, and effective. As a starting point in the development of a new approach, the City commissioned this discussion paper about the tools available to municipalities looking for ways to obtain amenity contributions from new urban development. This discussion paper explores the options available, examines the approaches used in some other communities, and addresses the issue of how amenity contributions affect the urban development marketplace, from the perspectives of landowners, developers, home-buyers, and tenants.

Coriolis Consulting Corp. specializes in urban land economics, market and financial feasibility analysis for development projects, growth management policy, and city planning. We have advised many communities on obtaining amenity contributions from urban development projects and we frequently assist in negotiating such contributions from individual projects. We have completed several comprehensive studies for local governments and developers about development levies, amenity contributions, and their impacts on the real-estate market.

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## 2.0 Scope of this Discussion Paper

Discussions about obtaining amenity contributions from development projects often become heated because not far below the surface of the discussion there are political and economic viewpoints about the “right” balance between private sector development rights and public sector regulation, about who ought to reap the benefit of increases in land value due to rezoning, and about the appropriate roles of private developers and municipalities in building communities. These issues must be examined to make headway in the development of a comprehensive, systematic, and (most importantly) widely accepted approach to community amenity contributions.

To provide as much light on the subject as possible, this discussion paper starts from the basics and attempts to provide an objective, thorough review of the role of amenity contributions in the development of communities.

The discussion paper proceeds as follows:

- The paper starts with a brief overview of the fiscal pressure that is at the root of municipal interest in obtaining amenities from urban development projects.
- Next, the document summarizes the main available approaches for obtaining infrastructure, amenities, or cash from urban development projects. This section relates these approaches to the legislative context for BC, setting out the legal basis for different approaches to obtaining contributions.
- Third, before getting into details about the advantages and disadvantages of different approaches to obtaining amenity contributions, the paper tackles two fundamental questions that are often asked by municipal Councils, developers, and landowners: Why should new urban development projects pay for community amenities at all? What is the impact of these contributions on the marketplace and, in particular, who really absorbs the cost?
- Fourth, to provide real-world examples of current practice, the policies and procedures of a few municipalities in BC and Alberta are outlined.
- Fifth, the advantages and disadvantages of the basic options for obtaining amenity contributions are presented and some suggestions for a comprehensive, integrated policy are outlined.

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### 3.0 The Starting Point

Every growing community has a unique set of growth management and fiscal pressures, but the “costs of growth” issue is almost always framed along these general lines:

- Municipalities accept urban growth in order to provide more housing and to accommodate employment, for reasons that include enhancing the local economy, increasing the diversity of housing stock to meet the needs of changing demographics, or to help achieve regional planning objectives. More residents (to support local businesses) and more jobs (implying a growing economic base) are generally seen as a good thing, provided that the associated urban development does not create unacceptable impacts.
- Urban development requires infrastructure and amenities to meet the needs of new residents and businesses. New infrastructure and new amenities impose capital costs (either paid upfront or borrowed and repaid over time) and ongoing operating costs.
- One way to raise revenue for the capital and operating costs of infrastructure and amenities is property taxes. However, there is almost always strong pressure from existing residents and businesses to avoid property tax increases. Consequently, most municipalities set property tax rates to cover operating costs, provide for a modest contribution to reserves, and generate some funds for capital expenditures, but not to cover all of the capital costs associated with growth. Municipalities use combinations of current general revenue (which is mostly property tax), accumulated reserves (most of which is accumulated from past operating surpluses), debt (which is repaid using property tax revenue), grants from senior governments when these are available, or special sources (such as casino revenues) to pay for some of the capital costs of building and maintaining the community. There are some specialized mechanisms whereby taxes can be levied only on the properties that benefit from certain new infrastructure or amenities. These are explored briefly in Attachment B. However, these mechanisms tax all properties in a defined area, whether or not the properties are redeveloping, so they are not, strictly speaking, a means of obtaining amenity contributions from new development. These mechanisms also require municipalities to obtain (usually by borrowing) the capital to create the amenity and then recover the cost over time via taxes. This is quite different than obtaining upfront amenities or capital contributions from new development projects.
- These various sources are not usually enough to cover all of the capital costs of growth, so municipalities need to look elsewhere for funds. For most Councils there is a compelling logic to the argument that new development causes the need for (and

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enjoys the benefits of) new infrastructure and new amenities, so new development should contribute to the cost. In addition to seeming logical, this has the optical appeal of suggesting to voting taxpayers that new development is paying its own way and not placing a tax burden on existing residents.

- Reluctant to push up tax rates but sensitive to criticism that imposing too much infrastructure and amenity cost on new projects makes development less viable or makes housing less affordable, Councils try to find an acceptable balance. They try to be supportive of new development and community growth while ensuring that new development makes a fair contribution to the costs of growth, thereby assuring existing residents that they are not somehow subsidizing developers.

It is the struggle to find this balance that has led municipalities to explore various ways in which new urban development can shoulder a reasonable share of the costs of growth (recognizing that “reasonable” is in the eye of the beholder).

The practice of seeking amenities or financial contributions from urban development projects has become common in BC, but it is not universally accepted as an appropriate way to finance the costs of community growth. Some developers and development industry organizations blame municipal levies or expectations of amenity contributions for increasing the cost of housing. Some say it is unfair to charge new development for amenities that benefit, and ought to be funded by, the whole community. Some say it is discriminatory to make new residents pay for community amenities or services, although existing residents usually counter this by saying it is not fair that they bear the burden of new services for “new” people.

There is an ongoing evolution in what is regarded in BC as a reasonable level of amenity and infrastructure contributions from development projects. Current practice in the City of Vancouver and a few other large municipalities that are struggling with the effects of growth is very different from what it was twenty years ago and is also very different from the current practice in many small communities that want growth and do not want to impose any costs that could be characterized as an obstacle to new development.

The rest of this discussion paper is founded on the following world view about the issue of financing the costs of urban growth:

- Urban growth requires capital investment in infrastructure and amenities to meet the needs of additional residents and businesses.
- Municipalities will use a combination of funding sources to pay for the capital cost of growth. Some of the capital costs will be funded by property tax (or tax-supported debt), senior government grants, and special revenue sources (e.g. casino funds).

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Like it or not, municipalities will also look to new urban development projects to contribute to infrastructure and amenities, so that they can demonstrate that existing taxpayers are not paying for new development. In doing so, they will make full use of their legislative powers and they will also tend to push the envelope, looking for ways to generate revenue that may not be explicitly allowed but are not explicitly prohibited.

- The pragmatic question, therefore, is not whether new urban development projects will contribute to infrastructure and amenities, but how can municipalities best design an approach to obtaining these contributions that is effective, fair, reasonable in financial terms, and avoids undesirable impacts on the market, particularly on the price of housing or space that accommodates employment.

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## 4.0 Basic Approaches to Obtaining Amenity Contributions

This section provides an overview of the main approaches that municipalities in BC use to secure contributions from new development projects.

The available mechanisms for obtaining contributions from development projects can be divided into two categories:

- Methods to obtain direct cash contributions from projects, regardless of whether rezoning is involved.
- Methods that use the zoning process to obtain contributions from projects.

### 4.1 Direct Cash Contributions Independent of Zoning

The two most basic tools for obtaining contributions to community infrastructure involve payments by developers. One of these is the direct provision of (or payment for) works and services (including in some cases the provision of land) and the second is the direct payment of contributions to community-wide infrastructure.

The most direct way in which new urban development contributes to the capital cost of growth is via the *provision of works and lands*. In BC, municipalities routinely require development projects to pay directly for works and services that are needed to serve the development and to require projects to contribute land for parks. The legal authority to require works and services associated with lands proposed for subdivision and/or development is clearly spelled out in the Local Government Act (Section 938), which allows municipalities to require development projects to pay for the hard infrastructure (such as roads, water, sewer) that is directly attributable to the development.<sup>1</sup>

The legal authority to require dedication of park land as a condition of subdivision is set out in Section 941 of the Local Government Act, which enables municipalities to require the dedication of up to 5% of land area for open space.<sup>2</sup> However, this tool is not typically applicable in a downtown context, in which most new development does not involve subdivision.

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<sup>1</sup> Local Government Act [RSBC 1996] Chapter 323. Part 26, Division 11, Section 938.

<sup>2</sup> Local Government Act [RSBC 1996] Chapter 323. Part 26, Division 11, Section 941.

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The provision of works and services and the dedication of land for park have been part of the development approvals process in BC for many years. They are well understood, not politically contentious, universally used, and completely straightforward. Therefore, this form of contribution is not considered further in this discussion paper.

Another common way that municipalities in BC obtain cash contributions from new development is to impose *levies on new urban development projects* to pay for community infrastructure, such as the Development Cost Charge (DCC), which is provided for in Sections 932 to 937 of the Local Government Act.<sup>3</sup>

Levies are cash payments made by developers to municipalities, for the purpose of contributing to the provision of community-wide infrastructure.

DCCs are the most common development levy in BC. DCCs are a mechanism whereby individual development projects contribute to the cost of community-wide infrastructure. The amount of the DCC is determined by detailed engineering and parks-related analysis of future servicing requirements and detailed planning analysis of the capacity for additional development, such that each new development project contributes a reasonable pro rata share of the cost of providing necessary expansion or upgrading of basic infrastructure. DCCs can be collected from residential, commercial, and industrial projects but not from tax-exempt institutional uses.

DCCs can only be collected in BC for roads, water, sewer, drainage and park land acquisition (and limited park land improvements). The funds must be expended on the purpose for which they were collected and within the defined DCC district in which they were collected.

The idea of charging DCCs is widely accepted in BC, although there are sometimes debates about the appropriate amount to charge and about the impacts of DCCs that are deemed (usually by the development industry) to be too high.

DCCs will continue to be an important component in local government efforts to obtain funds for infrastructure, so this discussion paper assumes they are an important component in a comprehensive approach. However, as Victoria already has a DCC system in place and has recently engaged in a review of its DCC system, this discussion paper does not address these in any detail.

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<sup>3</sup> Local Government Act [RSBC 1996] Chapter 323. Part 26, Division 10, Section 932– 937.

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## 4.2 Zoning-Related Contributions

The second category of approaches to amenity and infrastructure contributions is based on zoning. There are two main tools in this category:

- Amenity or density bonus zoning
- Voluntary amenity contributions at rezoning

### 4.2.1 *Amenity Density Bonuses or Zoning for Amenities*

*Amenity zoning, or density bonus zoning* as it sometimes called, is formalized in Section 904 of the Local Government Act.<sup>4</sup> Amenity zoning allows very broad scope to use zoning regulations as a means of obtaining amenity contributions from developments.

Zoning regulations typically define the allowable uses, maximum density, maximum height, parking requirements and other parameters for urban development. Often, an extra layer of regulation such as a development permit system gives a municipality additional control over design, such as landscaping, siting, exterior materials and colours, in order to ensure that new projects are a good fit in the neighbourhood or appropriate to an environmentally sensitive site.

Basic zoning (on sites already zoned for the intended development) and development permit regulations generally do not involve much negotiation, other than over details. The regulations give a high level of certainty to land owners, developers, planners, Council, community members and real estate agents about the development capability of a site. As a result, the market understands how to value land based on its zoning and residents know (or ought to know) what sort of redevelopment they might expect on any given property. The flip side of this certainty is that there is little scope for providing incentives to developers to help meet community needs and there is no mechanism to require or persuade developers to make a contribution to amenities or infrastructure (other than via direct works and services charges, land dedication at subdivision, or the collection of levies such as DCCs).

Density bonusing adds a new dimension to basic zoning regulations. Rather than simply define an allowable maximum density, density bonusing provides for a base or outright density that can be achieved without providing any special contribution and also

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<sup>4</sup> Local Government Act [RSBC 1996] Chapter 323. Part 26, Division 7, Section 904.

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provides for additional development rights that can be earned by providing certain amenities.

As a simplistic example, under traditional zoning a site might be zoned to allow an FAR of 3.0.<sup>5</sup> In a density bonus system, the site might be zoned to allow FAR of 3.0 if no amenity contribution is provided but to allow an FAR of 5.0 if certain conditions are met. These conditions might include providing an on-site amenity.

The Local Government Act (Section 904) sets out the municipal ability to link allowable density to the provision of amenities.<sup>6</sup> This section in essence says that a zoning district can specify one allowable density of development that is generally applicable in the zone and may also specify higher allowable densities that can be achieved if certain conditions are met. These conditions involve the provision of amenities.

Section 904 indicates that an amenity zone should specify the “number, kind, and extent”<sup>7</sup> of amenity that is to be provided. This language suggests that amenities should be well-defined, should be in the form of an actual physical amenity (such as a public open space, social housing, day care facility, public art, arts facility), and should be provided on the development site that is providing the amenity. Because some municipalities almost immediately saw the possibility of defining “amenity” as a “cash contribution toward an amenity”, the Provincial government has issued clarifying guidelines,<sup>8</sup> which include:

- The amenity should benefit the area in which it is located (i.e. it should help improve the neighbourhood in which the new development is adding people and putting a load on existing amenities).
- Density bonuses should not be used to fund infrastructure that should be funded by property taxes, Development Cost Charges, or other mechanisms that are intended to fund normal community infrastructure.
- Municipalities are discouraged from using density bonuses as a means of raising cash and are advised that a bylaw simply requiring the payment of money in exchange for development rights could be declared invalid. However, the guidelines recognize that there are cases in which it is impractical to provide an amenity on a

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<sup>5</sup> FAR stands for Floor Area Ratio, which is a measure of development density. A site zoned for FAR 3.0 is allowed to develop an amount of floorspace that is 3 times the area of the site (i.e. a 10,000 square foot site would accommodate 30,000 square feet of space).

<sup>6</sup> Local Government Act [RSBC 1996] Chapter 323. Part 26, Division 7, Section 904.

<sup>7</sup> Local Government Act [RSBC 1996] Chapter 323. Part 26, Division 7, Section 904.

<sup>8</sup> Ministry of Municipal Affairs and Housing, “Density Bonusing: A Guide and Bylaw”. March 1997.

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specific development site and note that there is value in having a means to enable several projects to pool their contributions to achieve a larger amenity than any one project could sustain. So, the guidelines suggest that a cash-in-lieu approach can work if municipalities are careful to define the purpose of, and the reason for, cash-in-lieu. Some municipalities have an explicit cash contribution component in some of their amenity bonus zones.

The essential ingredients of an amenity zoning regulation are as follows:

- The zoning defines an amount of development (i.e. density) that is allowed without providing an amenity contribution. Arguably, this base density should be enough to allow a viable project but this is not always the case.
- The zoning defines an additional amount of development that can be obtained if the project provides an amenity contribution. The contribution is either set out in a schedule or negotiated.
- Developers have the option of developing the base density (without making a contribution) or developing the larger project by providing the required amenity.

Implementing an amenity zoning scheme requires a change to the zoning bylaw. There are two broad alternatives for doing this. One approach is to rezone sites on a case-by-case basis, creating for each project a Comprehensive Development zone that defines (for that site) the achievable density and the required amenity. The other approach is to define zoning districts, with specific density and amenity provisions, that are applied to large areas. The case-by-case approach allows the amenity contribution and the associated density to be determined for individual sites. The district approach allows a formula to be in place that applies to many properties.

#### **4.2.2 Voluntary Contributions at Rezoning**

This is the approach to obtaining contributions that offers the greatest flexibility and the greatest opportunity to obtain public benefits from development projects, but it also has the potential to generate the most negative reaction on the part of the development industry.

The basis for this approach is that *municipalities have the discretionary authority to rezone or to not rezone property and that rezoning typically results in an increase in land value and the creation of a profitable development opportunity*. Consequently, the rezoning process creates an opportunity for municipalities to use their rezoning power to bargain for the “voluntary” provision of amenities.

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There are two very different perspectives on whether this is reasonable. Critics call this system “blackmail” or “selling zoning”. They argue that the contributions are not really voluntary (because the zoning is unlikely to be obtained without the contribution) and that the perception that zoning is for sale undermines the validity of community planning.

Developers also sometimes argue that the rezoning process involves risk and cost, so the benefits of a successful rezoning should belong to the developer, not “taxed” away by the municipality.

The alternative perspective is that municipal Councils have an obligation to consider the fiscal impact of growth when considering a rezoning application. If a proposed project will impose unacceptable capital cost burdens on the community, Council can reasonably deny the application. On the other hand, if a proposal benefits the community and does not impose any capital cost burden, the rezoning may be acceptable. In support of this perspective and of the idea that developers should pay (in the form of amenity contributions) for additional development rights conferred via rezoning, it should be remembered that developers are not bound to buy land that requires rezoning; they can instead purchase sites already zoned for development. A developer acquiring development rights via rezoning should not, in this line of thinking, expect to pay a lower total land cost (including the land purchase price, the cost of rezoning, and any amenity contribution to the municipality) in the rezoning route than would be paid to buy already-zoned land at market value.

The expectation of voluntary contributions (paradoxical as that sounds) is on the rise. Some municipalities have explicit targets, in some cases documented, for the amount of voluntary contribution that is expected from different types of rezoning and others have clearly established procedures for negotiating the nature and value of voluntary amenity contributions on an application-by-application basis. There are still places in BC in which this approach would (for now) be regarded as unconscionable and contrary to the natural order of the zoning and development process, but there are other places where this approach is business as usual; developers understand the system (and the rationale behind it) and they find the system reasonable to work with, while not necessarily agreeing entirely with it.

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## **5.0 The Two Most Frequently Asked Questions about Amenity Contributions: Why Should New Development Pay for Community Amenities? Who Really Absorbs the Impact of These Costs?**

### **5.1 Why Should New Development Make Amenity Contributions?**

While community growth brings benefits, it also imposes capital costs on local government to meet the needs of new residents and new businesses. Some of these costs are for hard infrastructure (such as roads, water, and sewer) or parks that are essential to serve new development. There are clearly defined, commonly used mechanisms such as Development Cost Charges to pay for these. While there may be arguments about the amount of DCC charges, hardly anyone still contends that they are inappropriate in principle. In a sense, DCCs simply provide developers with a highly organized system to share the off-site servicing costs that are necessary to support new development.

The DCC system has many advantages: it is clearly defined in legislation; explicitly applied; levied on all new development whether or not rezoning is involved; and the rates are set in an open, analytically rigorous fashion.

However, there is more to a community than streets and plumbing. Neighbourhoods need fire stations, recreational facilities, and libraries. While these are called amenities, which perhaps gives the impression that they are frills, they are important components of a complete, attractive, functional, safe (and marketable!) community. They must be provided in areas that are expected to absorb more residents and places of employment at higher density.

In BC, DCCs cannot be used for these kinds of community facilities. Arguably, if DCC legislation were overhauled to allow DCCs to be collected for a wider (but still reasonable) array of amenities, there would be less need for and less interest in other approaches to obtaining contributions. However, DCCs are limited to basics, so the money for other amenities must come from somewhere else. As noted already, local governments are reluctant to pass these costs, many of which are generally perceived as being “caused” at least in part by growth, onto existing residents in the form of increased property taxes. Senior government grants are almost never sufficient.

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So, there are at least four answers to the question “why should new urban development contribute to community amenities?”:

- The amenities would not be needed (or at least “less” amenity would be needed) if the new development were not bringing in new residents and businesses that need the amenities.
- The amenities can contribute to the attractiveness of the neighbourhood, which can increase the marketability and value of the residential or commercial space in the development. For this reason, developers are sometimes more supportive of making contributions to amenities that will be created in the short term than contributions to future amenities that will not be in place until after their projects are completed.
- In circumstances in which there is neighbourhood opposition to new development and densification, amenities can be a means to address resident concerns. This may seem more like buying off the opposition than enlightened civic policy, but it can be an important part of the rationale for associating new amenities with new development.
- In the end, it is neither the developer nor the end-user of the developer’s product that pays the cost of the amenity contribution, if the amenity contribution is set at the appropriate level. The effect of the amenity contribution is to lower land values. This is the most important answer to the question and it is also the most technically complex, so it is addressed in detail in the next section.

## **5.2 Who Really Pays?**

Before a municipality considers expanding its use of the tools for obtaining amenity contributions, it is important to understand the interaction between these costs and the urban development marketplace: Who is really impacted by the cost of amenity contributions? What is the impact of expecting developers to make voluntary amenity contributions when land is rezoned? Do these costs and contributions discourage development?

While developers actually write the cheques to pay for levies or amenity contributions, and while it is widely perceived (erroneously) that such costs are simply added on the cost of new development, making prices higher and exacerbating an affordability problem, the actual situation is both more complex and less harmful than it is often made out to be.

Whether a municipality raises funds via Development Cost Charges, obtains amenities from a density bonus zoning regulation, obtains amenities via voluntary contributions at

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rezoning, or uses all of these approaches, the primary effect is to put downward pressure on the value of development sites.

This section focuses on the market impacts of amenity contributions. The impacts of levies (such as DCCs) are similar in principle, but different in some important details, so they are not addressed in detail in this paper.<sup>9</sup>

To show how the cost of amenity contributions is absorbed in the real estate market, some simple hypothetical case studies are used, for amenity bonus situations and for rezoning situations.

### **5.2.1 Amenity Bonus**

Exhibit 1 shows a simplified version of a financial analysis of a multifamily residential development project, under three different scenarios. The numbers in Exhibit 1 reflect current market numbers in Downtown Victoria for unit sales prices and development costs.

Scenario 1 assumes a site of 20,000 square feet that is zoned to allow an FAR of 3.0, with no requirement for an amenity contribution. The gross development area is 60,000 square feet, which works out to about 60 housing units.

The numbers in the first scenario are organized to show that the developer sells the units, deducts the costs of constructing the units (including an allowance for paying a DCC), deducts a standard target for profit (15% of revenue) and calculates the maximum price that can be paid for the development site. In this case, the maximum land value that can be paid is \$2,400,000, which works out to \$40,000 per unit.

Scenario 2 assumes that the developer buys a development site that is already zoned to allow a maximum FAR of 5.0, which allows the development of 100 units, with no requirements for an amenity contribution. In this case the developer's profit is still 15% of revenue, although the dollar amount of profit is larger because the project is larger. The amount the developer can pay for land is still \$40,000 per unit, but the total land value has increased to \$4,000,000 because the development potential of the site is greater.

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<sup>9</sup> Attachment A discusses the market/financial impacts of levies for interested readers. The bottom line is that levies put downward pressure on land values for redevelopment sites. As long as the levy is not so large that it reduces the amount of land available for redevelopment, there is no impact on the profitability of a development project, no impact on the pace of development, and no impact on end-users such as homebuyers. There is an impact on land-owners, who will see the value of their sites fall, more or less by the amount of the levy.

Scenario 3 assumes that the site is zoned to allow for amenity bonus density. The site has an outright FAR of 3.0 (60 units) but the density can be increased at the developer's option to FAR 5.0 if the developer makes an amenity contribution. In this scenario, the value of the amenity contribution is set to \$4 per square foot of additional space (or about \$40,000 per unit in this case). This amount could either be the actual cost of providing an on-site amenity or it could be a cash-in-lieu payment that contributes to the creation of an amenity in the neighbourhood; in either case it has a cost to the developer of \$1,600,000.

EXHIBIT 1: AMENITY BONUS

	Scenario 1	Scenario 2	Scenario 3
Revenue	\$25,500,000 (60 units @ \$425,000)	\$42,500,000 (100 units @ \$425,000)	\$42,500,000 (100 units @ \$425,000)
Less Costs:			
Marketing @ 5% of Revenue	\$1,275,000	\$2,125,000	\$2,125,000
Hard and soft costs including DCCs	\$18,000,000 (60 units @ \$300,000)	\$30,000,000 (100 units @ \$300,000)	\$30,000,000 (100 units @ \$300,000)
Less Profit @ 15% of Revenue	\$3,825,000	\$6,375,000	\$6,375,000
Less Amenity contribution	\$0	\$0	\$1,600,000
Equals Supportable Land Value	\$2,400,000	\$4,000,000	\$2,400,000

These simple illustrations support three key observations:

- In Scenario 3, the requirement to make an amenity contribution has no impact on the sales price of the units. The developer has not added the cost of the amenity to the selling price (in a competitive market, a developer is a price-taker and any attempt to arbitrarily add an extra amount to the price, which is set in the marketplace by the interaction of supply and demand, will result in purchasers buying elsewhere). The purchase price is not affected by how the developer acquired the development density (by paying the previous land owner in Scenario 2 or paying the previous land owner and paying the City for the extra density, in Scenario 3). The one circumstance in which the price of the units might rise is if the amenity that is provided is so attractive that the marketability of the area and the project goes up. This would happen even if the amenity were funded by the municipality, though, so it is not an impact of the developer's financial contribution per se.
- The developer's profit is the same in Scenario 2 or 3. The fact that an amenity contribution was made in Scenario 3 is not relevant to developer's profit. The profit is larger in Scenarios 2 and 3 than in Scenario 1, showing that there is an incentive

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for the developer to use the amenity bonus system to go from FAR 3.0 to FAR 5.0 even if an amenity contribution is required.

- The value of the land in Scenario 3 is the same as in Scenario 1, because in both cases the land has outright density of FAR 3.0. The developer's total land-related costs, however, are the same in Scenario 2 (the site zoned FAR 5.0 is worth \$4.0 million) and Scenario 3 (the site is worth \$2.4 million for FAR 3.0; the price of the additional FAR 2.0 is the amenity contribution of \$1.6 million; the total cost of the development rights to \$4.0 million).

So, did anyone lose? The answer depends on how the site in Scenario 3 became zoned for the density bonus. If the site was previously zoned to allow FAR 5.0 but downzoned to an outright FAR of 3.0, the land owner lost value (from \$4.0 million to \$2.4 million). If the site was previously zoned to allow FAR 3.0 and rezoned to provide for an increase to FAR 5.0 with an amenity contribution, the land owner neither gained nor lost (either way the landowner has a site whose value is based on the outright density of FAR 3.0). If the site was previously zoned industrial or residential at FAR 2.0 and rezoned to residential via the density bonus scheme, the landowner has actually gained value by moving to residential at FAR 3.0 (although the gain is not as much as if the land were rezoned to an outright FAR of 5.0). Note, however, that if land trades at a value that already capitalizes in the value of rezoning (which can occur in a market where developers and landowners are used to getting rezoning without any requirement for amenities), the market must make an adjustment.

The numbers show that there is a way to make density bonusing a win from all perspectives:

- Housing purchasers gain because there is more product on the market as a result of more development capacity. They also gain because of the creation of amenities that would otherwise not exist.
- Developers can gain because they can earn more profit (albeit with some more market risk) by building larger projects on a given site.
- Landowners can gain if an upzoning is involved (although they gain less than they would under a rezoning in which development rights are conferred without an amenity contribution).
- The municipality and the community win by gaining an amenity at no capital cost.

## 5.2.2 Voluntary Contribution at Rezoning

Exhibit 2 uses the same basic approach as Exhibit 1 to show the effects of a developer making a voluntary amenity contribution in connection with the rezoning of a site. For ease of comparison with the previous example, the same size of site and same development project are used.

EXHIBIT 2: VOLUNTARY CONTRIBUTION AT REZONING

	Scenario 1 (Buy an already-zoned multifamily site at market value)	Scenario 2 (Upzoning an industrial site; no amenity contribution)	Scenario 3 (Upzoning an industrial site; voluntary amenity contribution)
Revenue	\$42,500,000 (100 units @ \$425,000)	\$42,500,000 (100 units @ \$425,000)	\$42,500,000 (100 units @ \$425,000)
Costs:			
Marketing @ 5% of Revenue	\$2,125,000	\$2,125,000	\$2,125,000
Hard and soft costs including DCCs	\$30,000,000 (100 units @ \$300,000)	\$30,000,000 (100 units @ \$300,000)	\$30,000,000 (100 units @ \$300,000)
Land cost	\$4,000,000	\$1,000,000	\$1,000,000
Cost of rezoning	\$0	\$200,000	\$200,000
Extra land development costs	\$0	\$1,500,000	\$1,500,000
Amenity contribution	\$0	\$0	\$1,100,000
Developer Profit	\$6,375,000	\$7,675,000	\$6,575,000

In this case, the site is assumed to be zoned for industrial use and is assumed to be regarded by the municipality as a good candidate in planning terms for conversion to residential use. The site could, for example, be part of an older industrial area that is no longer suitable for industry but is a good location for a high density residential neighbourhood. Because the prospect of rezoning is looked on favourably by the municipality, the rezoning process in this case is not perceived as having high risk.

The hypothetical site in Exhibit 2 is the same as in Exhibit 1; it has an area of 20,000 square feet and is assumed to have the potential for residential development (after rezoning) up to an FAR of 5.0, yielding 100 units.

Scenario 1 provides a base case, showing how the numbers would look if the developer bought an already-zoned site of similar size and development capability. As shown, the developer pays \$4 million for this land. Note that this is identical to Scenario 2 in Exhibit 1.

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Scenario 2 shows how the numbers look if the developer acquires an industrially used and zoned site at an industrial land value (based on current zoning) and is then successful in obtaining rezoning to multifamily residential at FAR 5.0 with no amenity contribution. Note that there are additional costs, as compared with Scenario 1, to rezone the land and to make the conversion from industrial to residential (such as cleaning up contaminated soil, demolishing old buildings, providing additional off-site services). Even after absorbing these extra costs, the developer's project becomes more profitable than in Scenario 1. In effect, the developer is now earning profit from two sources. First, there is the typical profit associated with developing the 100 units. In addition, there is the gain in land value as a result of rezoning. The developer earns this gain, in this case, because the previous land owner was willing to sell the site at an industrial price.

Scenario 3 shows how the numbers work if the developer makes a voluntary amenity contribution as part of the rezoning. In this scenario, the developer's profit is closer to the profit in Scenario 1. In effect, the municipality has captured almost all of the lift in land value that is caused by the rezoning. The numbers show the possibility that a share of the lift is left in the hands of the developer, as an incentive, which is why the profit is slightly higher in Scenario 3 than in Scenario 1.

Key observations based on these numbers are:

- As in the previous example, there is no effect on the price of the units. Purchasers pay a price that is set by the market and are blind to the developer's land cost and how it was paid.
- The developer's total land-related costs are very similar in Scenarios 1 and 3. In Scenario 1, the developer pays the land cost (\$4.0 million) to only one party, the previous land owner. In Scenario 3 the developer pays the land cost to several parties (\$1,000,000 to the previous owner, \$200,000 to consultants and the City to get the land rezoned, \$1,500,000 to environmental consultants and contractors to get the site cleaned up and development ready, and \$1,100,000 for an amenity contribution, bringing the total to \$3.8 million; the last \$200,000 is retained by the developer).
- The original land owner does not benefit in this case from the rezoning (other than being able to sell the land, which might have been harder if there was not developer interest). Note that the numbers as shown assume that the developer pays industrial land value for industrial land and does not pay the land owner any portion of the anticipated lift in value. If the developer "overpays" for the land, there would be a diminished ability to make an amenity contribution. It may be that the developer

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needs to pay some premium over industrial value to persuade the former land owner to sell, which would reduce the dollars available for the amenity contribution.

- The net effect of the amenity contribution in Scenario 3 is to make the project perform financially the same on rezoned land as it would on already-zoned, development-ready land as in Scenario 1.

### **5.2.3 Conclusions**

The examples are intended to show that it is possible to structure an amenity contribution system so that there is no impact on end-users (the people who buy units or lease commercial space), there is no negative impact on the profitability of development, and there is a positive impact on sellers of land. This result requires that the amount of the amenity contribution is directly linked to the lift in land value associated with the extra density that is obtained either via the amenity bonus schedule or the rezoning.

The amenity contributions do not come out of normal developer's profit. The amenity contributions derive from the payment by the developer for new development rights conferred by rezoning.

Essentially, in a density bonus system or in a rezoning, the municipality is conferring new development rights that have value. The developer acquires these rights (just as though the developer were acquiring zoned land) by providing an amenity. It works the same whether the developer pays cash-in-lieu or provides a physical amenity (as long as the cost of the amenity is similar to the value of the density being provided).

In the examples provided, the "price" of additional density is set more or less at its full market value. Some municipalities set the amenity contribution at less than full market value, in the hope that this will provide a greater incentive to developers. This does not usually work out this way, though, as the land market is very good at capturing this extra incentive if the density bonus system is built into existing zoning schedules rather than negotiated on a case-by-case basis at rezoning. If municipalities price bonus density that is defined in a zoning district at less than its market value, the benefit usually flows to land owners in the form of higher land values; under-pricing the bonus density does not ultimately result in an incentive to developers or lower prices for end-users.

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## 6.0 Current Municipal Examples

This section provides some brief descriptions of current practices in a few communities. These are not detailed case studies; they simply summarize some key aspects of how selected municipalities are using the tools available to them to obtain amenity contributions from development projects.

### 6.1 Vancouver

The City of Vancouver's development regulation powers flow from provincial legislation called the Vancouver Charter, not from the Local Government Act, so its approach to amenity contributions is not completely applicable to other BC municipalities, but Vancouver's approach is in principle the same as in municipalities under the Local Government Act.

Vancouver uses four main approaches to obtain amenity contributions:

#### Levy

The City charges a Development Cost Levy (DCL) on all new development, regardless of whether rezoning is involved. The DCL functions just like a DCC, although Vancouver is allowed to charge the DCL for different types of community infrastructure than are covered by DCCs. The DCL varies in different parts of the City.

#### Voluntary Amenity Contributions from "Standard" Rezoning

Vancouver defines a class of rezonings as "standard" if they meet certain tests (generally small sites outside of downtown that do not involve a transition from industrial use). These rezonings are expected to make a voluntary amenity contribution (which is called a Community Amenity Contribution or CAC) which currently works out to about \$3 per square foot of additional approved floor space (beyond what was permitted under the previous zoning). These contributions are used to fund libraries, public art, day care and other amenities. No special analysis is required for determining the contribution, which is calculated in much the same way as a DCC would be. Strictly speaking, this is a voluntary contribution; in practice all rezonings involve making this payment.

#### Voluntary Amenity Contributions from Non-Standard Rezoning

These are rezonings of large sites, sites in downtown, or sites involving a transition away from industrial use. In these cases, the City expects a Community Amenity Contribution

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at rezoning but the nature and value of the amenity contribution is negotiated on a case-by-case basis. The approach is essentially simple, although it can involve considerable technical and financial analysis. The City estimates the land value before the rezoning and after the rezoning (after deducting all costs associated with achieving the rezoning) to calculate the lift in land value. The expected voluntary CAC is more or less equal to this net lift in land value. The contribution can take the form of land for parks, non-market housing, on-site facilities, cash, heritage building preservation, or some combination. The total value of the contribution can be very large, depending on the size of the site, the approved density of development, the mix of uses, and the location (which affects land value).

The analysis required to support the negotiation process usually includes engineering (for development costs), market analysis (to gauge the sales performance of the real estate product being created), and financial analysis to determine “before” and “after” land values. The City does this work in-house or in some cases retains consultants.

The developer and the City engage in a process of informal negotiation to arrive at a package of public benefits that is mutually acceptable.

### Heritage Density Bonus

The City has a special approach to creating incentives to preserve heritage buildings. The City can grant a density bonus to a developer who commits to upgrade and retain a heritage building. The value of the bonus is based on the difference between the financial performance that would have been achieved by redevelopment and the financial performance achieved by the restoration. In effect, the owner is compensated for the money left on the table by keeping the building. The compensation is in the form of development rights (i.e. density). Because most heritage properties in Vancouver do not have the ability to accommodate extra development on site, the heritage bonus is classed as “transferable”. This means the developer is entitled to sell the development rights to other developers (in a defined area) who want to develop projects that are larger than they could develop on their own properties based on existing zoning.

Managing this transferable density system requires considerable expertise. City staff or consultants calculate the amount of development rights required for a heritage project. This amount is a function of the performance of the project (i.e. how much financial help it needs) and the going market price for transferable density. This density trades on the market: developers with “receiver” sites (that are eligible to take on more density) buy the development rights from the owners of heritage properties. The City monitors in a general way the total volume of development rights being created and the amount being taken up to ensure that the market stays near equilibrium, but the City is not directly

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involved in any of these transactions. If the City flooded the market by approving too much transferable density all at once, the market price would fall and heritage project developers would not see the transferable density as an incentive.

The amount of transferable density available for sale at any given time is usually referred to as the “density pool”, but this term is misleading in one respect. The density is not mingled into a single pool under the control of one party (e.g. the City). The “pool” is simply the sum of the transferable development rights owned by all land owners and available for sale to developers on eligible receiver sites, much as there is a “pool” of condominium units for sale at any given time.

Developers who want to buy density must seek out property owners who have density for sale. They negotiate a price and the density is legally transferred from one site to another.

The City has defined an area in which properties are allowed to receive density. Within this area, sites can develop to up to 10% more space than allowed by zoning, without going through a rezoning process, if the extra space has been acquired as transferable density.

## **6.2 New Westminster**

Before about 2004, the City of New Westminster had an informal policy regarding voluntary amenity contributions. The City anticipated that developers seeking rezonings would make a voluntary amenity contribution which was pegged at about \$1,000 per residential unit.

Since 2004, the City has adopted a more comprehensive and systematic approach to voluntary amenity contributions.

For significant rezonings, the City negotiates a voluntary amenity contribution on a case-by-case basis. The City’s expectation is that voluntary amenity contributions will be approximately equal to the value of the lift in land value that is associated with the rezoning. In some cases, the City looks for non-monetary contributions (e.g. high quality public open space), but the aim is that the cost of these amenities plus any financial contribution should be equal to land value lift. The lift is determined in a case-by-case process in which the City and its consultants conduct a financial analysis, present this analysis to the developer, and work toward mutual agreement on the appropriate amount of a voluntary amenity contribution. Since adopting this approach, contributions have increased to an average of more than \$3,000 per unit plus significant other non-monetary amenities.

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The City applies the same approach to voluntary contributions associated with some development variances. Variances that allow additional height that enables projects to utilize a larger proportion of their permitted density or variances that relax parking requirements (which reduce development cost) are looked to for a voluntary amenity contribution that is commensurate with the value of the variance. The incentive for developers is that they can make their projects more marketable (e.g. more view) and more efficient (e.g. avoiding an extra level of underground parking). The amount of the contribution is negotiated, but it is mainly determined by comparing the value of the site with and without the variance. As with rezoning, if the variance results in a lift in land value, a portion of this lift becomes the amenity contribution.

The City also currently makes limited use of density bonuses, in which some zoning districts allow additional density in exchange for the provision of specific amenities.

### **6.3 Surrey**

Surrey uses amenity zoning to obtain amenity contributions that help to create new communities. When Surrey completes a Neighbourhood Control Plan for a large new urban community, it rezones property into zoning districts that have a built-in provision for amenity contributions.

For example, land zoned for rural, low density use can be upzoned as part of the planning process, to a category that allows multifamily residential. The zoning district allows a limited amount of outright residential potential, but enables the developer to increase density (to a prescribed maximum) by making contributions in accordance with a specific schedule that is included in the bylaw. Cash contributions are required for park development (not park land acquisition, which is funded by DCCs), library, police and fire services, and community facilities. Consistent with the requirements of the Local Government Act, the required amenity and the received density are spelled out in detail. Surrey uses a cash-in-lieu system that allows contributions from many projects to be pooled for the creation of amenities that would be too large or too expensive for any individual project to provide.

### **6.4 Burnaby**

Burnaby uses an approach to amenity zoning in which properties must be rezoned to a Comprehensive Development District.

The CD zone prescribes an outright allowable density and an additional maximum amount of density that can be obtained by providing an amenity contribution.

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The eligible amenities are listed and include open space, public facilities such as a library, and public art. There is not a provision for cash-in-lieu.

The “amount” or value of the amenity contributed is determined as part of the CD rezoning process.

## **6.5 City of North Vancouver**

North Vancouver has a policy in its Official Community Plan that anticipates the provision of additional density in exchange for the provision of public benefits. The granting of additional density requires that each site be rezoned and it is during the rezoning process that the amount of additional density and the value of the contribution are negotiated. The negotiations are based on an analysis of the financial value associated with the rezoning.

The City allows density to be transferred to another site if the purpose is to preserve a heritage building.

## **6.6 Calgary**

The City of Calgary has had for many years a system of density bonuses in its downtown. The City’s Land Use Bylaw (equivalent to a Zoning Bylaw) prescribes outright densities that are allowed in the downtown districts and then prescribes additional density that can be obtained in exchange for providing certain project features. Historically, these project features were all physical features that were to be incorporated within the project, such as indoor or outdoor public plazas, connections to the City’s network of overhead, enclosed pedestrian pathways, or certain design features. The system is partly formulaic and partly negotiated.

Over the last couple of years, Calgary has been revising its approach to provide much greater flexibility.

A new community plan for a near-downtown neighbourhood called Beltline (in which the City wants to encourage higher density residential redevelopment) outlines a new approach to density bonusing along these lines:

- Sites are zoned for an outright allowable density that can be achieved with no amenity. These outright densities match existing zoning, so no properties are being downzoned.

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- The zoning allows for additional density that can be obtained in exchange for amenities that include: sustainable building features; affordable housing contributions; public art; and heritage building preservation.

The bonuses are a combination of formulaic and negotiated.

The City is about to embark on a process to completely revise its downtown density bonus system along similar lines.

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## 7.0 Developing an Approach to Obtaining Amenity Contributions

### 7.1 Density Bonuses

#### *What Conditions Must Exist for a Density Bonus System to Work?*

There are a few “must haves” to allow a density bonus system to work:

1. Developers must believe that the increased project size is marketable, physically feasible, and financially attractive. Extra density only has value to a developer if there is a market for the extra space, if the extra space is profitable, and if the increase in density does not produce a diseconomy (e.g. forcing a shift from wood frame to concrete construction, or forcing a partial extra level in an underground parking structure).
2. The extra density must be capable of being physically accommodated on sites without unacceptable impacts on urban design, neighbourhood character, traffic, or other factors that will cause opposition to the project or to the overall redevelopment plan for the area.
3. The price paid to the City for the density bonus (whether in cash or in the form of an amenity) should be more or less equal to the market value of the additional development rights. Theoretically, the maximum price is likely the prevailing market value of density (or say 90% of this value, assuming there are some transactional costs to incorporate the extra space in the plan for the project). If the extra density is offered for a cash payment of much less than market value, it is likely that sooner or later land owners will end up getting any value that the City had hoped would be an extra incentive to developers. There are circumstances in which a municipality could obtain more than market value for additional density if the additional density allows an economy of scale or if the developer is willing to pay more than market value to obtain the necessary political and community support for a project. This is unusual and could only be ascertained on a case-by-case basis.
4. The City and the community should perceive that the amenity received is sufficient to make it worth absorbing the extra density into the neighbourhood.
5. The City must know what objectives it wants to achieve. Whether the aim is cash, heritage building retention, on-site amenities, or certain project characteristics, the system requires that the City articulate in advance what must be provided in exchange for density. Presumably, in defining its objectives, the City takes into account the needs of the community, the implications of new public amenities for

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ongoing operating costs, the responsibility for maintaining the amenity, and the means of securing the amenity for the long-term.

If, for example, the City wants day-care capacity to be provided, the City must think through whether it wants to own the space (presumably via strata title) and who will actually operate the day-care.

6. The combination of allowable base density and the price charged for bonus density must result in an acceptable number of sites being financially viable redevelopment candidates. If the achievable densities are too low (or the total cost of the density is too high) to support a redevelopment site value that is higher than an existing use site value, development will not be financially viable and developers will not be able to participate in the density bonus system. In an already-developed area, there will always be a mix of sites that are development candidates and sites that are not. If a city plan is looking for redevelopment and densification, it is important to have a realistic sense of how much new product the market could take up each year and then ensure that the appropriate amount of land is financially viable for redevelopment based on allowable densities.
7. Redevelopment sites must actually trade in the market at a value founded on their base density, so that developers can afford to pay the City for the bonus density. This is a key point and it has significant implications for how Council handles rezonings and how the City prices bonus density.

If landowners and developers have the perception that they can obtain rezonings without going through the density bonus “system”, they will capitalize the value of upzoning into land prices and there will be no financial room for amenity contributions. Council must be consistent in not granting rezonings (within the area in which amenity bonusing is being used) that are outside the density bonus system. Developers must see that the density approach is being consistently and universally (within the applicable area) applied so that they do not overpay for land and then argue that they cannot afford an amenity contribution. The situation in the Beltline neighbourhood of Calgary is a good illustration of the problem. Prior to the introduction of density bonus policies and regulations, developers could routinely obtain rezoning from density in the range of FAR 5.0 to density in the range of FAR 10.0 or more without making amenity contributions. Consequently, redevelopment sites traded at values reflecting the easily achieved higher upzoned value. For the new density bonus system to work, land owners and developers must learn that FAR 5.0 really means 5.0, and that any additional density can only be obtained via the density bonus system, not via rezoning outside the system. There will be a transition period in which landowners must adjust their expectation of value to match value under existing zoning, developers must learn to pay for land based on its existing

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allowable outright density, and Council must consistently decline to approve upzonings outside the prescribed density bonus route.

### ***Advantages and Disadvantages***

The amenity bonus approach has several advantages:

- It is predictable for landowners and developers (because it is defined in a bylaw).
- It is consistent across projects in the same zone.
- It is easy to administer, and can be designed so that there is little or no negotiation (because the required amenity contribution is specified).
- It is voluntary, in that developers can choose to develop only up to the base density or can seek extra density. It should be noted that this approach would become non-voluntary if the base entitlement is set unreasonably low.

To the extent that amenity zoning is designed to be negotiable on a case-by-case basis, the administrative complexity (and cost) goes up, but the flexibility to achieve a greater array or more individual tailoring of amenities is increased.

The only disadvantage to amenity bonusing is that it can limit flexibility because so much of the system must be spelled out in the bylaw, unless the bonus is determined on a case-by-case basis which really means the system is more like voluntary contributions negotiated during rezoning than like the formulaic approach to density bonus that is anticipated by the Local Government Act.

### ***What Kinds of Municipal Objectives are a Good “Fit” with the Density Bonus Approach?***

A density bonus system is essentially a quid pro quo transaction: the developer gives the amenity or cash and the City gives the extra density. To some extent, therefore, bonus density systems work best when the value of the density being conferred is readily determined and the cost of the amenity or other benefit being provided is readily quantified.

Here are some general observations about different kinds of municipal objectives and their “fit” with the density bonus approach:

1. *The broad goal of neighbourhood densification.* Densifying neighbourhoods can contribute to community goals for sustainability by increasing transit efficiency, achieving enough trade area support for a full network of local retail and service businesses, and reducing suburban development. A bonus density system can help

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achieve the goal of densification if the system is structured so that it encourages developers to use the available higher density.

2. *Revenue for community amenities.* Density bonus systems are suited to obtaining revenue in a cash-in-lieu system to pay for community-wide amenities that require contributions to be assembled from many projects or sources of funds. The system lends itself to the creation of a schedule of the charge for each additional square foot of development potential that can be obtained.
3. *Specific on-site amenities.* Density bonuses can be used to achieve specific on-site amenities such as public open space, affordable housing, public art, or on-site community facilities such as library or day care space.

One challenge with this use of bonus density is that it is harder to compare the value of the extra density (which is easy to determine) with the cost of providing the amenity (which may be much harder to determine, as the nominal cost may not be the actual cost). For example, it is easy to calculate the nominal cost of an outdoor plaza, but some of this cost may have been absorbed in site landscaping anyway and some of the cost may be recovered by the developer in the form of higher selling prices or rents, such that the real cost is lower than the nominal cost. It could be argued that the relationship between value of the bonus density and cost of the amenity should not matter, as long as the developer is happy with the numbers and the City gets the amenity it wants. However, the overall long term success of the system depends partly on it being predictable and equitable to all participants so it is important that the relationship between density value and amenity cost be somewhat consistent across projects.

4. *Specific project characteristics.* Bonus density systems can also be used to provide incentives for projects to achieve specific characteristics. For example, the City could confer extra density on projects that achieve certain urban design objectives or that use “green” building technology or achieve LEED certification. The City could provide density incentives to mixed use projects that exceed some minimum requirement for combining retail, office and residential use.

As with on-site amenities and heritage building preservation, the challenge is to figure out the relationship between the value of the density provided and the amenity granted. A system that offers bonus density for a wide range of possible project characteristics will tend to be skewed toward the characteristics that cost the least. It is easier to administer a density bonus for project characteristics that are self-evident and can be secured in advance of construction. For example, a density bonus for mixed use can be secured via land use and the permits make it clear what the mix of use is before construction. LEED certification, on the other hand, is not confirmed until construction is complete. What happens if bonus density is granted and constructed, but the building fails to achieve certification?

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The system can be designed to achieve any or all of these objectives. The more objectives that are on the table (that is, the more options there are for developers to obtain density in exchange for different amenities), the harder it will be to design a system in which outcomes match the City's priorities, unless there is detailed work done to calibrate the granting of density to the actual cost of providing different amenities.

### ***What Elements are Needed to Make Sure a Density Bonus System is Efficient?***

One of the potential advantages of density bonusing over rezoning, as a means of securing amenities, is that density bonusing can be more efficient. This efficiency depends on a few key features that must be built into the system:

1. The City should try to make the system as well-documented and predictable as possible. Density bonus schedules (base density, maximum allowable additional density, amenities to be provided) should be explicitly defined in the land use designation. There should be limited negotiations on a site-by-site basis, as this defeats the purpose of having an efficient and easy-to-administer system.
2. There should be a minimum amount of subjective evaluation required in the approval process. The provision of the amenity should not involve interpretation (is this mixed use or isn't it? Is this building "green" enough to qualify?) The density system must define in advance what conditions must be met to qualify for the additional density.
3. The process should not require rezoning (after the initial amendment to put the density bonus system in place), so that developers see the benefit of a lower risk and more efficient approval process to obtain the extra density.
4. Properties should not be down-zoned. Ideally the density bonus is in addition to the development that would have been achieved under the former zoning. This is not because municipalities are not allowed to down-zone (they are), but because it is sure to create a hostile reaction on the part of landowners. Implementation is smoothest if landowners and developers see the system as not diminishing allowable density but creating a vehicle for getting more density.

### ***Are There Any Major Challenges or Problems Associated with Density Bonusing and How Can these be Addressed?***

There are some obvious challenges, including:

1. Deciding on the amenities to be achieved and whether the focus should be on revenue, on-site amenities, or project characteristics.

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2. Ensuring that the base density is set at the right level and that the density bonus is likely to be of interest to developers.
  3. Ensuring that the relationship between the value of the density and the cost of the amenity are acceptable to developers and to the City.
  4. Finding ways to build in real incentives to developers.
  5. Making sure that everyone understands the system and gets past arguments that the City is reducing developer profits or increasing the cost of new units to consumers.
  6. Finding appropriate ways to secure the amenity “in perpetuity”. This is not an issue if amenity contributions of cash are pooled to create a municipally owned amenity. However, if the amenity is on-site (e.g. art, affordable housing, day care), the municipality needs a way to take title to the amenity or otherwise ensure that it lasts.
  7. Maintaining and managing the amenity. Any amenity will need some kind of ongoing maintenance and management, so the municipality must plan to take this on or have a means of allocating the ongoing responsibility to another party.

There are some other challenges of a more philosophical and political nature.

One of these is the perception that a density bonus is selling zoning. A traditional view of development regulation holds that municipalities make land use decisions based on a variety of planning, engineering, environmental, and social considerations. Once determining the “right” uses, heights and density, municipalities designate land to allow appropriate development. In this traditional view, the land value conferred by the zoning designation belongs to the land owner; municipalities don’t get paid for the zoning because their role is to create the rules for development.

Density bonusing is somewhat at odds with this view. On the assumption that FAR 5 is an appropriate density for new development in a neighbourhood, setting the base density at what some would see as an arbitrarily low number such as FAR 3 seems to undermine the validity of planning. If the FAR 3 is the “right” density for the neighbourhood, don’t allow more density. Or, if FAR 5 is the “right” density, designate accordingly. The only way out of this box is the premise that there is no single right density. FAR 3 may be right for projects that do not contribute to the broader community, in the form of amenities or design or some other benefit, and FAR 5 may be the right density for projects that do contribute. To give validity to the planning process and have a functioning bonus density system, it is imperative to have a sound rationale for the base density, for the maximum density that can be achieved with bonus (as this maximum density must still be defensible in planning, engineering, environmental, and social terms), and for the conclusion that a specific bundle of amenities or benefits warrants the extra density. *If the upper limit on achievable density is arbitrarily high or*

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*the base density that can be achieved without amenity is arbitrarily low, the system risks appearing as though it is sacrificing community planning in order to impose an arbitrary cash grab on development.*

Another challenge is dealing with the perception that developers who contribute amenity contributions in cash should have a strong voice in deciding what to do with the money. There will be a tendency for developers to think that the contribution was “their” money (because they wrote the cheque) and that the City has an obligation to spend the money in a way that will benefit the projects that provided the funds. This argument forgets that the amenity contribution is not a tax or levy or gift; it was part of the developer’s land acquisition cost. Theoretically, the developer should no more expect to be able to influence how the City spends the money than the developer should expect to tell a land vendor how to spend the money from selling land. In practice, though, there will be a tendency to assume that any cash contribution will be spent in the area in which it was collected and spent on things that will benefit new developments and this assumption is reinforced by the language in the Local Government Act. A good case can be made for spending the money in the neighbourhood (as the rationale for the contribution is the need to address the costs of growth), but the city should not feel compelled to literally make amenity investments in ways that will only immediately and directly benefit the specific projects that made the contributions.

## **7.2 Voluntary Contributions at Rezoning**

Voluntary contributions at rezoning are far less codified than amenity bonuses. The total value of the amenity that can be offered by a developer depends in part on the overall economic performance of the redevelopment project (which often involves a change in land use and almost always involves an increase in density). In particular, the ability of a project to make amenity contributions is dependent on the lift in land value that results from rezoning. However, knowing the land value lift created by rezoning requires analysis. For rezonings that are large (in land area or total floor space), it is not appropriate to assume that all developers would have the same ability to make voluntary contributions or that all projects would be in a position to volunteer the same kinds of amenities. Sites with waterfront, heritage buildings, potential for park, or potential to accommodate a major recreational facility should make individually-tailored amenity contributions. Defining an appropriate voluntary contribution for these projects takes time and work on the part of the developer and the municipality, which must decide if the nature and value of the contribution is sufficient to offset the fiscal impacts of the growth. This effort can be justified for large, complex projects but may not be appropriate for small, straightforward rezonings that involve minor changes in use or density. However, there are municipalities that routinely negotiate amenity contributions on even small

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rezonings as they find that an investment in staff time and consulting fees to negotiate amenity contributions can be well rewarded.

The main advantage of this approach is the complete flexibility to define allowable density and amenity contributions for each site. The main disadvantage is that this flexibility comes with a cost, in terms of time and expertise needed to conduct negotiations and achieve a mutually acceptable package.

Voluntary contributions offered in support of applications for development variance permits are not common, but in principle could work the same as if a rezoning were involved. For example, a developer may be interested in exceeding the maximum building height prescribed by zoning, without obtaining a density increase (i.e. achieving a taller building with a smaller footprint). This alternative form may be more valuable (because more of the floor space has views), but may also have an impact on the neighbourhood (i.e. shading, impact on privacy, or view blockage). There could be a trade-off in which the developer provides a voluntary amenity to the neighbourhood in exchange for the height variance. This is not explicitly anticipated in the Local Government Act, but granting a variance is a discretionary act by Council so in principle the argument is the same as in a rezoning.

The use of voluntary contributions at rezoning or at the granting of a variance involves essentially the same challenges outlined above in the density bonus section.

### **7.3 The Special Case of Heritage Conservation**

Density bonuses for heritage conversation (whether formulaic or negotiated on case-by-base basis) have one unique element. Often, the additional development rights being conferred cannot be accommodated on the site of the heritage building. Therefore, a mechanism is needed to make the density transferable to other sites. Note that any transferred density is acquired (at market value) by the developer who uses it, so this extra density cannot also be expected to be linked with a new amenity contribution. Therefore, an area that is expected to absorb transferable heritage-related bonus density will have a constraint on its ability to also provide other amenity contributions.

### **7.4 DCCs**

Projects that are making voluntary amenity contributions or obtaining density bonuses also must pay DCCs. Because of the effect of amenity contributions and DCCs on the developer's ability to pay for land, in effect the higher the DCC the less room there is for an amenity contribution. Municipalities must look at the whole DCC and amenity contribution "load" on projects to ensure that development will remain financially

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attractive to developers and that developers will still be able to acquire development properties.

## **7.5 Integrated Approach**

The mechanics of any regulatory system should be derived mainly from a set of objectives: the municipality must be clear on what it is trying to achieve, in order to design a system that will have the desired result. A regulatory system should also be founded on a set of principles, to ensure that system is fair and reasonable.

The following principles are suggested as an appropriate foundation to an integrated amenity/ infrastructure contribution system:

- The system should be squarely within the legal boundaries set by provincial legislation.
- The system should be “administratively appropriate”: small, straightforward projects should not require expensive and time-consuming processes; larger, complex projects involving large sites, significant changes in land use, or large changes in total urban development capacity may reasonably involve a more complex process.
- The system should rely on incentives to the extent possible. Developers should be given reasonable options: develop under existing zoning or choose to seek additional entitlements (by changing land use or increasing density in exchange for making appropriate contributions to offset the costs of growth).
- The system should be reasonably consistent and predictable. This is certainly true of prescribed amenity bonus schedules. Even rezonings or variances involving site-specific negotiations should be conducted in accordance with a systematic approach and should reflect a reasonably consistent approach to defining an appropriate value of contribution and an appropriate roster of amenities to be provided.
- The system should be used to generate amenities or revenue to be applied to amenities that are linked to the costs of accommodating growth, not as simply a tax on development that is used to fund programs or facilities unrelated to the need for amenities or infrastructure imposed by growth.
- Amenities sought via a density bonus zone or volunteered by developers should be consistent with the City’s objectives for amenities and infrastructure as outlined in the City’s Official Community Plan or other planning policies.
- The value of the amenity or infrastructure contribution should be commensurate with the development value that is being conferred. If the amenity contribution is too expensive, developers will not be interested. If the contribution is too low, new development is providing a lesser share of the cost of growth than it is capable of

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sustaining. The balancing point is right where the developer is willing to apply for rezoning or use the amenity bonus, willing to make the contribution, and earns just enough additional revenue to justify the cost, time, and risk inherent in the process.

- The combined effect of DCCs and amenity contributions should be evaluated, to ensure that development is still financially viable and to ensure that the downward pressure on land value is not so great that the availability of development sites is reduced.
- The City must thoroughly think through issues such as ownership of amenities, responsibility for maintenance/repair, and responsibility for operation.

Each municipality must choose the extent to which it expects new urban development to make direct contributions of amenities and infrastructure. Each municipality must find the appropriate balance (at any given time) between levies such as DCCs, amenity bonus zoning, or negotiated voluntary contributions at rezoning.

The purpose of this discussion paper is to demonstrate that there are several mechanisms – that are reasonable, transparent, legal, efficient, and successful – that municipalities can use to obtain amenities and infrastructure from new urban development without having significant negative impacts on the pace of development or on the price of new residential or commercial space.

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## Attachment A: Impacts of Development Levies

There is a widespread perception that development levies can have a direct impact on the cost of new development and therefore add to the sale price or lease rate for new floorspace. Consequently, there is a concern that levies will directly cause residential or commercial prices to rise, which is generally regarded as an undesirable outcome.

A simple example can be used to illustrate the primary impact of a development levy such as a DCC.

The chart below shows a hypothetical multifamily residential development project, on an already-zoned site, before and after the introduction of a levy.

The chart shows a simplified version of how a developer would estimate how much to pay for a development site. In this case, the site has an area of 20,000 square feet and is zoned to allow an FAR of 5.0, which yields 100,000 square feet of space, or say 100 units.

	Before Levy	After Levy
Revenue (100 units @ \$425,000 per unit)	\$42,500,000	\$42,500,000
Costs:		
Marketing @ 5% of Revenue	\$2,125,000	\$2,125,000
Hard and soft costs (100 units @ \$297,000 per unit)	\$29,700,000	\$29,700,000
DCCs (\$3,000 per unit or \$3 per square foot)	\$0	\$300,000
Profit @ 15% of Revenue	\$6,375,000	\$6,375,000
Land Value	\$4,300,000	\$4,000,000
Land Value per unit	\$43,000	\$40,000

Here is what happens:

1. In a competitive marketplace, developers cannot simply add the cost of a levy onto the asking prices for new floorspace. Adding the levy on to the asking price would imply that purchasers are willing to pay more for “levied” space than they would pay for comparable space in comparable neighbourhoods with lower (or no) levies. This, of course, does not happen. Unless someone has a monopoly on a commodity, prices are set by the interaction between supply and demand; no supplier can

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unilaterally determine price simply because costs are higher. If the market values of these units were actually \$3,000 per unit higher, the developer would have been asking this price without the levy. In a sense, a levy in a particular area is no different than if the area had unusually poor soil conditions and therefore above average construction costs. Prices in the affected area will not be arbitrarily higher than in directly competitive areas simply because some development costs are higher. Something else must “give”.

2. While developers pay the levy when they obtain project approval, they will seek ways to transfer the impact to others, because developers require a profit margin to make development an attractive business. Being neither willing to absorb the levy as a reduction in profit nor able to simply add a surcharge on end prices for their products, the first response of developers to a levy is to lower the bid price for development parcels by an amount equal to the levy<sup>10</sup>. The primary impact of levies, therefore, is to put downward pressure on the value of properties for redevelopment. As noted earlier, this is no different than a developer’s response to the fact that an area has worse soils conditions than comparable areas. A developer will be willing to pay less for such sites, by an amount equal to the cost of remedial work (e.g., pre-loading, drainage, excavation, or extra construction costs) needed to make the net cost of the site equivalent to comparable land with no soils problems.
3. It is the land market’s response to the downward pressure on land value for redevelopment sites that mainly determines the ultimate impact of a new (or increased) levy. If the same amount of land remains available for new development projects (i.e., on the market at a price developers are willing to pay) after the introduction of a levy, broadly speaking the supply of new product to the market should be unchanged and there will not be an impact on the price of new

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<sup>10</sup> Urban land economists use a method called residual land value analysis to demonstrate this point, which is also reflected in appraisal methodology and in the way developers determine how much they can afford to pay for a particular site.

Total revenues from a proposed new project are estimated. These are assumed to be the same with or without a levy, as developers in a non-monopolistic market are price-takers.

Then all product creation costs (except land) are deducted. These include construction costs, professional fees, financing, and all permit fees and levies. Again, developers are price-takers. They cannot arbitrarily reduce the cost of building construction because they are required to pay a levy.

Next, the developer deducts an allowance for profit, which is budgeted as a target rather than left to chance as whatever happens to remain after project completion. Market forces tend to produce market-wide consistency in target profit levels (i.e. if profits are too low, some participants will leave the business, which over time will lead to higher prices and higher profits, as supply of new units will fall; if profits are too high, some new participants will enter the business).

Deducting all costs and targeted profit from revenue leaves the residual amount that a developer can afford to pay for land. This residual amount is reduced if unit sales prices fall or if any cost goes up, including the introduction or increase of a municipal levy.

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floorspace.<sup>11</sup> Developers experience the same total project cost (albeit made up of different line items) as they would face without the levy, the same amount of new development happens, and there is no reason for demand to change, so prices to consumers and profits for developers remain at pre-levy (or pre-changes to the levy) levels. Only the land value supported by redevelopment changes.

However, if the downward pressure on land value for development sites means that less land is available for new development after the levy (because the reduced offered price for land results in less land being available on the market), the supply of new product will be reduced. This leads to rising prices for all existing and new supply, not just for new floorspace.

4. The key to understanding and anticipating the impact of levies, therefore, is to understand how the levy is likely to affect the supply of land available for new development. This depends on the characteristics of individual properties, market conditions, the objectives of individual owners, and other factors.

At any given time, there is a pool of properties available for redevelopment for residential, commercial, or mixed use. Levies can cause a range of possible impacts on the size of this pool of properties available for redevelopment:

- a. the pool of redevelopment sites can be *increased* in cases where the levy is associated with a rezoning or an infrastructure upgrade that allows development that could not otherwise occur. In the case of rezoning, if the levy is a necessary cost of achieving the new zoning (e.g. increased density or more valuable mix of uses) and if the lift in land value due to rezoning is greater than the cost of rezoning including the levy, “new” land is available for redevelopment. In the case of an infrastructure upgrading (without rezoning), if the levy finances and facilitates upgrading that could not otherwise occur (or that could only otherwise occur with greater cost or greater complexity as the result of coordinated actions by individual landowners), additional land will be available for redevelopment. In this case, the levy effectively replaces an off-site cost that would have been absorbed in any case.
- b. the levy has a *neutral effect* on the pool of redevelopment properties in cases where the value of a given property as a redevelopment site is still higher, after deducting the amount of the levy, than the value of the property in its next most valuable possible use. As well, the levy has a neutral effect on the pool of available redevelopment properties in cases where even before the levy

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<sup>11</sup> There is one exception to this. If a levy is used to finance the creation of new or better amenities and services in a district, prices for space in this area could rise because the area has become more desirable. This is an impact of the amenities, not the levy per se, and it would be the same if the amenities were funded by property tax revenues or provided voluntarily by private developers, rather than funded by levies.

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properties were not candidates for redevelopment because they are too valuable in their present use.

- c. the levy *decreases* the pool of redevelopment properties in cases where the levy makes previously viable redevelopment less financially attractive than available alternative uses. For example, if redevelopment as residential supports a higher land value than continuation of an existing older industrial use before the introduction of the levy, but the levy tips the balance in favour of maintaining the existing use, a redevelopment candidate has been “lost” until such time as prices rise enough to warrant redevelopment under the new levy system.

Any new or increased levy can have a combination of these various effects (on different properties), so it is the net combination that determines the impact of a levy on the likelihood of redevelopment and on the ultimate price of new floorspace.

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## **Attachment B: Some Property Tax Mechanisms for Collecting Revenue from Specific Areas**

Property taxes are usually thought of as applying to the whole community, including existing development and new development. General taxes are not a means of obtaining revenue from new development, because general property taxes cannot single out new projects.

These are some mechanisms that allow municipalities to take a somewhat more targeted approach to property taxation, including Local Services Taxes and Tax Increment Financing.

Local Services Taxes are allowed under Sections 210 to 219 of the Community Charter.<sup>12</sup> The essential components of a Local Services Tax are:

- a specific service is defined and a specific benefiting area for this service is defined.
- Property owners within the benefiting area either approve the service plan (or do not successfully petition against the plan if it is initiated by the municipality).
- If approved, the municipality creates the service (using general revenue, reserves, or borrowing) and then levies an additional property tax on the properties in the service area.

As a means of obtaining amenities from new development, this has some obvious disadvantages. First, while the boundary of the service area could be drawn to include a high proportion of potential redevelopment sites, the new tax applies to all properties whether they are redeveloped or not. Second, the initial capital investment must still be made by the municipality and recovered over time. In the short term, this uses capital reserves or borrowing capacity. Third, there is not the flexibility to obtain amenities on development sites. A Local Services Tax is an effective way to finance an improvement that benefits a whole district but is not an effective way to obtain amenities directly from new development projects.

Another, much less common, use of property taxes to fund area improvements is called Tax Increment Financing. This is a mechanism whereby a municipality makes a capital investment in infrastructure or amenities in an area, on the expectation that this investment will attract new development and lead to increases in property value, and

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<sup>12</sup> Community Charter [SBC 2003] Chapter 26. Assented to 29 May 2003. Part 7, Division 5, Sections 210-219.

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then earmarks any increase in property taxes (increase over the base amount prior to the investment) to pay for the initial investment.

This mechanism is not a new tax; it is an allocation of increased taxes to pay for the investment that helped create the property value growth that resulted in the tax increase. Unless this mechanism carries within it the means to give the municipality access to tax revenues that would otherwise be paid to another agency<sup>13</sup>, there is no new money. Mainly, tax increment financing can be a way to facilitate municipal borrowing, in non-traditional ways such as bond issues, because the municipality pledges the tax increment to debt repayment.

Tax increment financing is not explicitly allowed under existing legislation in BC, but there are specific areas in which it has been approved. It is not a means of obtaining upfront amenity contributions directly from development projects.

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<sup>13</sup> For example, a tax increment financing scheme being used by Calgary will give the City access to any increase in School Taxes to pay for non-School capital projects in the special district.