



Inclusionary Zoning (IZ) Impact Assessment

Peer Review

February 22, 2024

Parcel



PREPARED FOR:

The Corporation of the City of Richmond Hill

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**Phoebe Chow**

Manager, Policy Planning

February 22, 2024

The Corporation of the City of Richmond Hill
225 East Beaver Creek Road, Richmond Hill, Ontario, L4B 3P4

RE: Inclusionary Zoning (IZ) Impact Assessment - Peer Review

Parcel Economics Inc. ("Parcel") is pleased to provide the City of Richmond Hill ("Richmond Hill", the "City") with the following peer review and written opinion of *Sub-Report 4: Inclusionary Zoning Impact Assessment* prepared by SHS Consulting ("SHS"). This previous SHS reporting was originally included as part of the broader *City of Richmond Hill Affordable Housing Strategy – Background Report*.

Based on our review and our own re-cast of selected elements of the analyses relied upon by SHS, it is our professional opinion that:

- The study **adequately addresses the underlying intent of the requirements** set out in *Ontario Regulation 232/18* with respect to the implementation of new Inclusionary Zoning programs at the time.
- Although the general methodology relied upon by SHS appears reasonable, **some assumptions may warrant updating and selected improvements could also be made** to further bolster the financial feasibility testing prepared. For example, hard and soft costs assumptions were likely underestimated at the time and the industry has further experienced substantial cost increases over the last several years (i.e., at rates well beyond those considered in the SHS analyses).
- Notwithstanding the foregoing, the **evolving policy context—namely, proposed amendments to Ontario Regulation 232/18 – materially alter the nature of the research findings and recommendations** contained in the original SHS reporting. Specifically, new limits to the inclusion—or "set aside"—rate to no more than 5% and affordable rental periods to 25 years, which are well below some of the inclusion rates supported by the SHS analyses in 2021. These policy changes, in and of themselves, likely necessitate a revisiting of the supporting analyses prepared.



Overall, we recommend that the financial feasibility testing prepared in support of IZ Impact Assessment be updated to further bolster the potential introduction of a new policy framework by the City of Richmond Hill. As detailed herein, these updates should generally focus on a combination of the following factors: (i) assumed preconstruction and construction timing; (ii) above and below grade hard cost assumptions; (iii) financing rates; and, (iv) application of discount rates.

The following report details the results of our independent, third-party review.

Sincerely,

Parcel

Parcel Economics Inc.

Chris White, PLE
Principal

Matt Paziuk
Principal



Table of Contents

1.0 Introduction.....	1
1.1 Background.....	2
1.2 Purpose.....	2
1.3 Scope.....	4
2.0 Review.....	6
2.1 Methodology.....	7
2.2 Inputs & Data.....	10
2.3 Interpretation of Findings.....	20
3.0 Conclusions.....	27

Table of Figures

Figure 2.1 "Assessing Impact of an IZ Policy" (Figure 82 of the SHS Study)	9
Figure 2.2 "Density Increase by MTSA" (Table 11 of the SHS Study).....	10
Figure 2.3 "Pricing and Unit Characteristics by MTSA" (Table 12 of the SHS Study).....	12
Figure 2.4 "Financial Assumptions - Hard Costs, 2020" (Table 14 of the SHS Study).....	13
Figure 2.5 Comparison of SHS Cost Assumptions to Altus Guide, 2020	14
Figure 2.6 Comparison of SHS Cost Assumptions to Altus Guide, 2020 vs. 2023.....	15
Figure 2.7 Statistics Canada Building Construction Price Index.....	16
Figure 2.8 "Maximum Inclusion Rates for Building Tenure Type 1" (Table 17 of the SHS Study)	21
Figure 2.9 "Maximum Inclusion Rates for Building Tenure Type 2" (Table 18 of the SHS Study)	22

1.0

Introduction

1.1 Background

In 2018, the Province of Ontario passed Regulation 232/18, which allow municipalities to implement Inclusionary Zoning (“IZ”) policies under predefined conditions and parameters.

IZ seeks to secure non-market housing as a by-product of broader market-based development. This policy tool has been implemented in many jurisdictions across the United States—to vary degrees of success—and the approach has more recently been actively studied and considered in many Canadian cities, including across Ontario.

In response to the above policy direction at the provincial level, the City of Richmond Hill commissioned *Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report* (herein referred to as the “IZ Impact Assessment”). The purpose of this study was to explore the expected impact on the local housing market of a potential IZ policy.

To complete this study, Richmond Hill retained the services of SHS Consulting (“SHS”), a consulting practice focused primarily on affordable and non-profit housing. As outlined in more detail herein, the SHS study was completed in March 2021, including a supporting research program, the preparation of financial pro forma analyses for a number of different submarket areas, consideration for a range of alternative scenarios or potential outcomes by way of corresponding “sensitivity analyses”, consultations with local real estate professionals active in the Richmond Hill market (i.e., the development community), and delivery of a complete report inclusive of all related research findings, conclusions and recommendations.

1.2 Purpose

Assessment Report

The IZ policies introduced by the Province under the *Planning Act* resulted in *Ontario Regulation 232/18*, which was filed on April 11, 2018. The study commissioned by the City and completed by SHS is ultimately intended to satisfy the requirement for the “*Assessment Report*” identified under this regulation and as part of the municipality’s

consideration for developing new Official Plan policies. As noted in the SHS IZ Impact Assessment, this Assessment Report is required to provide an “analysis of potential impacts on the housing market and on the financial viability of development or redevelopment in the municipality from inclusionary zoning by-laws”, specifically taking into account the following factors:

- **value of land;**
- **cost of construction;**
- **market price;**
- **market rent;** and
- **housing demand and supply.**

Written Opinion

The role of Parcel Economics Inc. (“Parcel”) for this assignment has been to ensure the underlying appropriateness, accuracy and suitability of the IZ Impact Assessment, thereby providing Richmond Hill with additional confidence in the findings and recommendations presented.

Specifically, *Ontario Regulation 232/18* requires a “written opinion on the analysis” described above that is prepared by a “person independent of the municipality and who, in the opinion of the council of the municipality, is qualified to review the analysis”. To this end, Parcel has been retained to undertake this peer review and written opinion of the SHS study in an effort to satisfy this measure and ultimately advance the implementation of the City’s potential new IZ policy framework.

Although the consideration for implementing IZ policies is a relatively new concept for Ontario municipalities and therefore only a selected few of these peer reviews have been completed to date, we note that they are commonplace in various other areas of land use planning and the municipal development approvals process. In

particular, they are perhaps most common as part of critiquing other types of land economics assignments, including market demand and impact studies and/or in support of dispute resolution (e.g., in preparation for Ontario Land Tribunal hearings, etc.). In our experience, these types of studies are typically intended to provide a municipality or other public sector organization with an **unbiased, third-party perspective and to further validate (or refute) the findings presented as part of an original research assignment.**

1.3 Scope

Core Elements

It is important to make clear the underlying extent and scope of our involvement with this assignment at the outset of this review. As established in the original terms of reference with the City, this review has generally been intended to address a number of core elements of the IZ Impact Assessment and ultimately to prepare the following key tasks/deliverables:

- Review the validity and overall appropriateness of the **underlying statistical research and supporting assumptions** utilized in the original report.
- Review of the **underlying approach and methodologies** utilized, with specific regard for the structure and format of the residual land value style pro forma analyses prepared in the context of supporting the implementation of the City's new IZ policy framework.
- Review and comment on the ultimate **interpretation of the research and analyses presented**, including the appropriateness of the resulting study conclusions / recommendations.
- Preparation of a **high-level "re-cast" of the financial assessment prepared**, to ensure the accuracy of all relevant calculations and back-end processing of the analysis.
- Engage in direct **correspondence with relevant members of the original project consulting team (SHS)** to ask questions, confirm assumptions and address other relevant items;
- Presentation of **additional independent commentary and/or insights** that may further substantiate (or refute) specific elements of the analyses prepared, based on our own professional experience and observations in conducting similar studies, both locally and in other communities across Canada.
- Providing our professional opinion as to whether—all things considered—the subject sub-report serves as an **appropriate means of estimating the feasibility of prototypical development projects**, as outlined.

- Where applicable, **determining whether any specific edits / updates / improvements to the analyses are required** prior to further advancement of preferred IZ policies (i.e., identification of any specific limitations or relevant matters that need to be highlighted in relying on the work prepared to date).
- Assessment and determination as to **whether the requirements of Ontario Regulation 232/18 have been met** by the background sub-reports prepared to date.

Meetings / Correspondence

In addition to the specific tasks identified above, we have also **engaged in ongoing and active discussions with municipal staff and appropriate representatives of SHS**, including liaising with relevant technical/analytical staff to clarify our understanding of the analysis and key data inputs, as needed.

Limitations & Exclusions

In light of the above scope of work, and as agreed upon with the City before undertaking this review, we further note that there are a number of specific exclusions and/or limitations to our review, including but not necessarily limited to the following:

- We have not validated the calculation of relevant development-related municipal fees and charges (e.g., development charges, planning application fees, etc.), which are all assumed to be sufficiently accurate for the purposes of this review and have already been vetted by the City of Richmond Hill.
- Beyond a high-level review of their general suitability and consistency with current development patterns, we have not provided a direct critique nor other commentary on the conceptual developments considered by SHS within each of the submarket areas identified (e.g., with respect to overall scale of development, densities, consistency with municipal policy and development permissions, etc.). We trust that these have all been appropriately reviewed and understand that they were established by SHS in direct coordination with municipal staff before being tested for viability.
- We have not prepared a detailed, line-by-line audit of the various financial pro forma analyses produced by SHS and all corresponding spreadsheets, cell references, etc. Instead, and respecting the propriety nature of many of these elements of the original study, we have undertaken a more high-level review and recast of sample pro forma analyses provided by SHS in a “pasted as values” spreadsheet format. Given that all of the distinct feasibility analyses and related sensitivities follow a similar—if not identical—analytical structure and format, these are generally assumed to be appropriately representative of the entire body of work prepared by SHS as part of this assignment.

2.0

Review

2.1 Methodology

The following details our high-level review of the methodology employed by SHS to evaluate the effects of introducing a new IZ policy framework on the financial feasibility of development in each Major Transit Station Area (“MTSA”), considering a combination of tenures (i.e., condo and rental) and affordability types.

Analytical Structure & Approach

In completing this type of community-wide feasibility analysis and ultimately informing future municipal policies, it is important to emphasize that no two development sites are the same and individual developers will have varying motivations and return expectations (or requirements) to consider when underwriting a new development project. This dynamic presents one of the single greatest challenges in assessing the impacts of IZ on the financial viability of development across broad market areas.

With this in mind, the following provides a brief overview of our review, understanding and commentary on the fundamental methodologies and approach adopted by SHS as part of their study.

- Four (4) MTSAAs were selected in collaboration with City staff to represent a variety of geographies, heights and densities. These included:
 - **Richmond Hill Centre;**
 - **Major Mackenzie;**
 - **Valleymede;** and,
 - **Bernard.**

- Again, in collaboration with City staff, two types of prototypical buildings were considered: (i) high-rise (11+ storeys) and mid-rise (5 - 10 storeys). These development concepts considered both purpose-built rental and condominium/ownership tenures in each MTSA submarket.

In our experience, although not without its pitfalls in terms of appropriately reflecting the potential unique conditions or requirements of individual sites, this general approach is certainly most common and can generally be considered an emerging “best practice” for such high-level, citywide analyses.

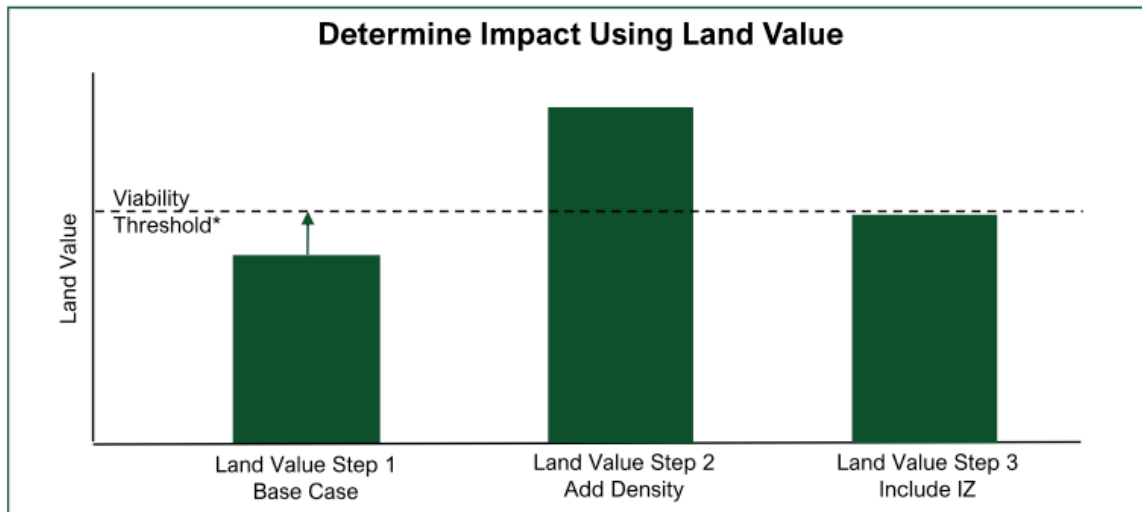
- Based on these prototypical developments, SHS assessed the financial viability of development using a residual land value (“RLV”) approach. As noted by SHS, *“The analysis assumes that if a development is financially feasible and sufficient money is left to acquire the land based on market prices, the developer can proceed with the project.”*

Often utilized in the development community as a “first pass” when underwriting potential development site acquisitions, an RLV assessment requires less detail and specificity than a more comprehensive discounted cash flow (“DCF”) pro forma modelling technique typically relied upon once a site has already been identified as having some underlying development potential. The latter DCF approach is generally more appropriate when a detailed site-specific development concept is being tested and optimized to ensure returns will be met and financing can be secured. As such, while this general approach will not necessarily guarantee the future feasibility of a given development project, it typically provides an appropriate measure of viability and economic promise at a much earlier stage such as this (i.e., as part of a municipal land use policy exercise such as this).

- SHS estimated the base value of the land in each MTSA based on a condominium tower as the highest and best use, and based on current height and density permissions. The resulting land prices per buildable square foot were compared to recent land transactions and conversations with developers.
- Next, to determine the “uplifted land value”, a second scenario was run with added heights and densities established for each MTSA, estimated in close collaboration with City staff. SHS notes, *“These estimates are based on the maximum uplift in heights and densities the City might be willing to allow in these areas.”*
- A third scenario was then run which incorporates the potential IZ Policy (e.g., proportion of affordable units, price of affordable units, period of affordability etc.).
- To evaluate the impact on land values and determine the viability of the IZ policy, the different scenarios were compared. **SHS deemed a development scenario viable if its RLV is about 10% or higher than the RLV of the base case scenario.** If it fell below 10% of the base case, SHS assumed that the project might not be viable because the landowner would not have sufficient motivation to sell the land. Figure 82 from the IZ Impact Assessment provides a graphical overview.

Figure 2.1

“Assessing Impact of an IZ Policy” (Figure 82 of the SHS Study)



Source: Figure 82 of Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report prepared by SHS Consulting.

Parcel Professional Opinion

Overall, we find this to be a **reasonable approach** for understanding the high-level implication of implementing IZ within each MTSA submarket.

We do, however, caution that it is unlikely that the prototypical base land values assigned to each submarket will be consistent with current landowners’ actual or perceived values in practice and/or on a more site-by-site basis.

2.2 Inputs & Data

Based on the general analytical structure set out in the previous section of this review, the following provides a more detailed overview of our findings with respect to several of the more specific sub-elements of the IZ Impact Assessment.

This includes the range of specific **inputs**, **assumptions** and **other statistical sources** relied upon to complete the subject analyses.

Development Concepts

Table 11 of the IZ Impact Assessment summarizes the prototypical site assumptions, including both current and maximum development densities, as expressed by Floor Space Index (FSI).

Figure 2.2

“Density Increase by MTSA” (Table 11 of the SHS Study)

MTSA	Building Type	Current Density (FSI)	Units in Tower with Current Density	Maximum Density (FSI)	Units in Tower with Maximum Density	% Change in FSI	% Change in Units
Richmond Hill Centre	Highrise	3.5	382	6.5	709	85.7%	85.6%
Major Mackenzie	Midrise	2	89	2.8	124	40.0%	39.3%
	Highrise	2.5	298	4	476	60.0%	59.7%
Valleymede	Midrise	2.5	79	3.2	101	28.0%	27.8%
	Highrise	2.5	222	4.2	373	68.0%	68.0%
Bernard	Midrise	2	126	3	189	50.0%	50.0%
	Highrise	4	534	5	667	25.0%	24.9%

Source: Table 11 of Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report prepared by SHS Consulting.

Parcel Professional Opinion

In our opinion, these assumptions appear **reasonable and reflective of both existing policies and emerging development trends** in each submarket. The general scale and nature of development contemplated is also consistent with our own professional experience in this part of the Province, including work directly on behalf of the local development community and other landowners / real estate investors.

Market Information

Financial model assumptions were developed prior to completing the pro-forma analysis. The assumptions are based on desk research, SHS Consulting's experience as development consultants, and telephone interviews with experts. The assumptions were verified with developers and key informants from Richmond Hill during two engagement sessions conducted as part of this background report. - Pg. 261, The City of Richmond Hill Affordable Housing Strategy – Background Report

Land Values

There are some inherent and unavoidable limitations to this type of demonstrative analysis in terms of potential disconnect between the land values modelled in the analysis versus the actual or perceived values for specific landowners throughout these areas. This is a distinct challenge of introducing any new IZ policy framework, whereby local landowners could be reluctant to acknowledge or accept downward pressures on land values. This reluctance to accept downward pressure on land values can be particularly strong for sites that currently may be worth more to the owners based on the existing income generating operations than the one-time payout of selling the site for re-development.

Furthermore, we also note that land values do tend to be more resilient to change or market fluctuation and generally exhibit a certain level of "stickiness" (less likely to respond immediately) relative to other forms of real estate pricing (e.g., price per square foot sales levels, which are more immediately responsive to changing market conditions or consumer preferences, land use policy amendments, infrastructure announcements, etc.). The resulting risk of this dynamic is that overall development activity is thereby reduced given the weakened financial prospects resulting from the lower revenue-generating opportunities inherently presented by non-market/affordable housing options.

As previously outlined, the values upon which all IZ scenarios were judged are at least 10% above the base case scenario. By comparing against a land value higher than base case and not expecting landowners to lower their land value expectations, SHS is mitigating against the challenges described above. However, we note that **some landowners are likely to have expectations more in-line with the “uplifted land value” calculated by SHS** and associated with the provision of additional density (i.e., commensurate and/or similar to the “Step 2” land value identified with density added in Figure 2.1 above).

Revenue Assumptions

Table 12 in the IZ Impact Assessment details the condominium and rental revenue assumptions utilized by SHS.

Figure 2.3

“Pricing and Unit Characteristics by MTSA” (Table 12 of the SHS Study)

MTSA	Unit Type	Unit Size	Condominium Pricing	Condo Fees	Market Rental Rates	Market Rental Rates	Parking Ratio*	Rental Parking Revenue
		sq. ft.	\$ per sq. ft.	\$ per sq. ft. per month	\$ per month	\$ per sq. ft. per month	stalls per unit**	\$ per month
Richmond Hill Centre (only high-rise)	1-bedroom	550	\$895	\$0.55	\$1,943	\$3.36	0.7	\$100
	2-bedrooms	750	\$800	\$0.55	\$2,625	\$3.17	0.8	
	3-bedrooms	1,050	\$790	\$0.55	\$3,045	\$2.43	1	
Bernard	1-bedroom	550	\$895	\$0.55	\$1,900	\$3.31	0.8	\$100
	2-bedrooms	750	\$800	\$0.55	\$2,400	\$3.20	0.9	
	3-bedrooms	1,050	\$790	\$0.55	\$2,800	\$2.18	1	
Major Mackenzie	1-bedroom	550	\$895	\$0.55	\$1,850	\$3.33	0.9	\$100
	2-bedrooms	750	\$800	\$0.55	\$2,500	\$3.34	1	
	3-bedrooms	1,050	\$790	\$0.55	\$2,900	\$2.81	1.2	
Valleymede	1-bedroom	550	\$895	\$0.55	\$1,900	\$3.31	0.9	\$100
	2-bedrooms	750	\$800	\$0.55	\$2,400	\$3.15	1	
	3-bedrooms	1,050	\$790	\$0.55	\$2,800	\$2.73	1.2	

Source: Table 12 of Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report prepared by SHS Consulting.

We note the following:

- Unit sizes, condominium prices and maintenance fees were estimated based on information collected from condominium developments selling in the market area at the time of the initial research and analysis undertaken. These assumptions appear reasonable based on our independent review of comparable data sources (e.g., Altus Data Studio).

- Market rental rates and parking rates were established based on an environmental scan of condominium rental prices and parking rentals collected from Condos.ca and verified with developers. Albeit somewhat atypical relative to other markets with a more robust supply of purpose-built rental buildings, SHS chose to focus on the secondary rental market (i.e., individually owned condominium units for rent) as no new purpose-built rental buildings have been built in Richmond Hill since 2012. Again, we believe this is a reasonable workaround given the circumstances.
- We note there is no variation by MTSA submarket for condominium unit sizes and prices, and very little variation for rents. Again, given that there is generally less market segmentation across the various subject MTSAAs identified within the City of Richmond Hill relative to other jurisdictions in which new IZ frameworks have been implemented, this is a reasonable approach and convenient for the purposes of simplicity and consistency across the different financial modelling provided.

Hard Costs Assumptions

The hard cost estimates were primarily derived from the Altus Construction Cost Guide (2020), though SHS also notes, *“Some assumptions were derived from recent comparable projects for which SHS acts as the development consultant”*. These costs are said to be validated with developers during engagement sessions held at the time too.

Figure 2.4

“Financial Assumptions - Hard Costs, 2020” (Table 14 of the SHS Study)

Hard Costs - Variables	Assumption
Apartment up to 12 storeys (per sq. ft.)	\$275
Apartment 13 to 60 storeys (per sq. ft.)	\$250
Underground Parking (per sq. ft.)	\$100
Contingency Factor (% of hard costs)	3%
Cost Inflater, per annum (% of hard costs)	2%

Source: Table 14 of Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report prepared by SHS Consulting.

Parcel Professional Opinion

Given the high-level nature of the development concepts considered and in the absence of more site or development-specific cost estimates from a quantity surveyor, we consider the hard costs in the Altus Guide **appropriate for inclusion in this type of RLV analysis**.

We note that the SHS assumptions are at the high-end of the Cost Guide 2020 range for apartments up to 12 storeys, near the bottom end of the Cost Guide 2020 range for apartments 13 – 60 storeys, and below the Cost Guide 2020 range for underground parking. When site-specific details are not possible, we typically **rely on at least the median of the Cost Guide range**.

Figure 2.5

Comparison of SHS Cost Assumptions to Altus Guide, 2020

Hard Cost Variables	SHS Assumptions	Cost Guide 2020	
		(Low)	(High)
Apartments up to 12 storeys	\$275 PSF	\$200 PSF	– \$275 PSF
Apartments up to 13-60 storeys	\$250 PSF	\$210 PSF	– \$310 PSF
Underground Parking	\$100 PSF	\$125 PSF	– \$170 PSF

Source: Parcel, based on the 2020 Altus Construction Cost Guide, GTA.

Furthermore, we note the Altus Guide rates are expressed on the basis of costs per square foot (PSF) of Gross Construction Area (GCA).

Using zoning floor areas to calculate costs is a common and potentially costly error. The Cost Guide rates are calculated using the Canadian Institute of Quantity Surveyors' definition of floor area, whereas zoning floor area definitions differ from municipality to municipality and often exclude significant areas of the building from the calculation. Thus, using the floor area measured per zoning definitions can result in underestimating costs by as much as 12%. If you do not have floor plans for your building

when preparing your budget, you will need to “gross up” the zoning floor areas to account for the variance in definition. – pg. 6, Altus Construction Cost Guide (2020)

Based on our review of the more detailed modelling prepared by SHS, it appears that SHS has assumed no difference between GCA and Gross Floor Area (GFA). GFA can differ across each municipality and often excludes portions of building areas. In By-law 111-17¹, these exclusions include mechanical penthouses, loading areas, parking structure or any space with a floor to ceiling height of less than 1.8 metres. For example, in the Richmond Hill Centre model reviewed the Net Floor Area was 85% of the Gross Floor Area, which is a common building efficiency assumption. However, if the GFAs analyzed by SHS are not consistent with GCA then **a further gross up may be warranted to appropriately estimate project total costs.**

Where Are Construction Costs in 2023?

Since the Cost Guide 2020 was published, hard construction cost estimates in the Guide have risen dramatically. Given the high-level nature of these types of analyses, in 2023 we would recommend hard costs of at least \$330 PSF for apartment up to 12 storeys, \$345 PSF for apartments up to 60 storeys, and \$235 PSF for underground parking levels.

Figure 2.6

Comparison of SHS Cost Assumptions to Altus Guide, 2020 vs. 2023

Hard Cost Variables	SHS Assumptions	Cost Guide 2020 (Low - High)	Cost Guide 2023 (Low - High)
Apartments up to 12 storeys	\$275 PSF	\$200 - \$275 PSF	\$275 - \$380 PSF
Apartments up to 13-60 storeys	\$250 PSF	\$210 - \$310 PSF	\$285 - \$400 PSF
Underground Parking	\$100 PSF	\$125 - \$170 PSF	\$195 - \$270 PSF

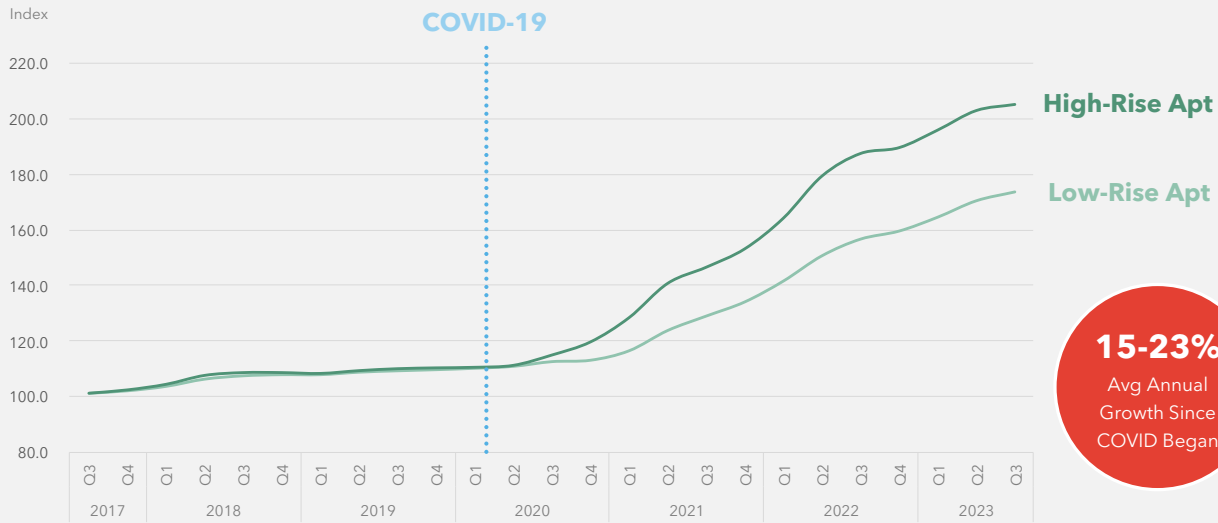
Source: Parcel, based on the 2020 and 2023 Altus Construction Cost Guides, GTA.

This is echoed in Statistics Canada Building Construction Price Index data, which illustrates **15 - 23% average annual growth** in construction prices since Covid began at the end of Q1 2020.

¹ Yonge and Bernard Key Development Area Secondary Plan Zoning By-law

Figure 2.7

Statistics Canada Building Construction Price Index



Source: Parcel, based on the Statistics Canada Building Construction Price Index for High-rise apartment buildings (5+ storeys) and Low-rise apartment building (< 5 storeys).

Although not included in the IZ Assessment Report, additional discussions with SHS revealed an assumed construction period of 30 months and no assumption for pre-construction activities related to the 50-storey building typology in Richmond Hill Centre. We note that this may be a somewhat aggressive timeline, both in the context of assumed pre- and during-construction periods. Details of our own recommended development timelines will be captured as part of the update to Sub-Report #4 of the Background Study for the City’s Affordable Housing Strategy (completed in parallel and delivered under separate cover).

Parcel Professional Opinion

Given construction costs have risen well above the 2% per annum assumed in the SHS analyses, Parcel recommends **updated pro forma analyses be undertaken to account for drastically higher construction costs** utilizing assumptions more in-line with the current Construction Cost Guide ranges.

Soft Cost Assumptions

Municipal development fees (including planning application fees, building permit fees, development charges, community benefits charges, parkland contributions, and property taxes), which make up a large portion of soft costs, have been included by SHS as direct inputs from the City. Other soft costs (i.e., professional fees, site related studies, legal, administrative expenses, marketing, and financing) have been estimated as a percentage of hard costs based on typical “rule of thumb” type ratios, a common technique across all real estate pro forma analysis.

Although not detailed in the IZ Impact Assessment, our review of the more detailed modelling provided by SHS confirmed that additional costs—such as HST—were also included. Our more detailed review also revealed some soft costs which were excluded or, in our opinion, underestimated (e.g., architecture & engineering costs, marketing costs, construction management, development fees).

Parcel Professional Opinion

In our opinion, SHS undertook an appropriate level of detail in terms of the specific “line items” and specific variables considered in the pro forma analyses, which is consistent with the level of detail commonly utilized by Parcel (i.e., notwithstanding any differences in the underlying analytical structure and methodologies applied to certain calculations).

Nonetheless, consistent with our observations above, we believe that these assumptions should be **updated to reflect current market conditions**.

Other Assumptions

In addition to the more targeted market-based assumptions identified above, the RLV models prepared by SHS require several assumptions that must go beyond what today's market research reveals and therefore incorporate an element of professional judgement. These include:

Capitalization Rates (Cap Rates)

Combined with the net operating income (NOI) expected from the new buildings, capitalization rates—or “cap rates”—are used to estimate an income-producing asset's value upon completion and stabilization. Market cap rates across all asset classes are readily reported on for both current and historical periods, however, future cap rates are unknown and must be forecast based on the modeler's best estimate of future market conditions and expected investment returns.

The cap rates utilized by SHS are generally in-line with past and current cap rates reported in the Region and, in our opinion, are reasonable to assume over the short- to medium-term in the City. However, there may be an opportunity and rationale to adjust the relativity of the cap rates between market and affordable rental uses, albeit unlikely to materially affect the outcomes of the financial analysis.

Revenue and Cost Growth

The RLV models utilized by SHS involve consideration for market conditions over future periods and as such, current market revenue and cost assumptions were assumed to grow into the future. Specifically, SHS has conservatively assumed that revenues and costs will grow by some 2% annually on a go-forward basis.

We appreciate this conservative growth rate (by comparison to recent/historical patterns) and believe that by assuming revenues and costs will grow equally, the future value of development land is not reliant on growth in market demand (i.e., revenue growth) outpacing the corresponding growth of costs, which would then speculatively add value to land into the future. We do note that because revenues represent a larger dollar amount overall, a 2% growth rate for revenues and costs will result in a larger amount of growth in dollar terms for revenues than hard construction costs, meaning revenue growth will slightly outpace cost growth in dollar terms.

Developer's Profit

A key component of any RLV model is to account for, and preserve, a reasonable developers' profit. SHS has identified a total of 15% of project revenues to reflect this opportunity for profit-generation. It is important to note that—although developers often do not achieve the targeted profit margin included in their RLV upon completion of a development project—assuming anything less at this early stage of the development process would not allow for

the real world “wobble room” that development projects often need to see them through more detailed site-specific planning processes and execution.

This, in effect, serves to reflect an appropriate contingency or “buffer” on any profit margins, thereby allowing for potential future fluctuations (increases) in costs, poor sales performance and/or other potential unforeseen circumstances. Furthermore, a healthy profit margin ensures that projects will secure financing in terms of presenting more favourably to prospective lenders.

Discount Rate

SHS has applied a 6% discount rate to future rental cash flows and developer profit expectations to estimate their present value. Although 6% is consistent with other similar studies undertaken in 2020 / 2021, we note that if an analysis is using a present value approach then the discount rate should be applied to all cash flows, including condominium sales, development costs and developer’s profit expectations, as all of these occur many years into the future.

Parcel Professional Opinion

Based on the foregoing observations relating to technical assumptions predicated more on professional judgment and discretion, we have identified a number of ways in which the pro forma modelling could potentially be improved as part of future updates.

Although these will have varying levels of impact on the actual results and findings of the analysis—very limited, in some cases—these include: (i) **adjusting cap rates across market and non-market (affordable) residential uses**; and (ii) **applying discount rates more consistently across all cash flow elements identified in the pro forma.**

2.3 Interpretation of Findings

As is the case with any land economics assignment of this nature, it is important to not only ensure the quantitative methods and underlying calculations, assumptions and statistical inputs are sound and appropriately representative of potential real-world conditions, but also to validate the resulting interpretation of the analysis and any key takeaways and recommendations. That is, the analysis needs to go “beyond the numbers” and achieve some substance in more practical vs. theoretical applications.

The following focuses on providing a supplementary and independent review of the resulting conclusions and recommendations contained in the IZ Impact Assessment. This primarily focuses on the **maximum inclusion—or “set aside”—rates identified** as being feasible in the Richmond Hill context.

Additionally, we have provided a more general discussion around a number of key themes gleaned from the experience(s) of other Ontario municipalities in implementing new IZ policy frameworks (i.e., flexibility, timelines for policy implementation, monitoring, balancing strategic priorities, etc.).

Proposed Amendments to Ontario Regulation 232/18

Posted on October 25, 2022 the Province has proposed amendments to O. Reg. 232/18 (Inclusionary Zoning) to “provide more certainty/clarity and make inclusionary zoning rules in Protected Major Transit Station Areas more consistent across the province”. Key changes proposed include:

- A **maximum requirement of 5% of total units** (or 5% of the total gross floor area of total residential units, excluding common areas) be set aside as affordable.
- A **maximum period of 25 years** over which affordable units would be required to remain affordable.
- The approach to determining the lowest price/rent that can be required for IZ units would be **80% of the average resale purchase price** of ownership units OR **80% of the average market rent** for rental units.

In the proposed amendment the Province states, “The proposed changes would provide more development cost certainty and establish a more consistent approach to inclusionary zoning requirements across the province. It would also support government priorities to provide housing that is affordable and within reach of more Ontarians.”

Maximum Inclusion Rates

Scenario #1: Condominium Towers with Affordable Ownership Units

SHS recommends a maximum inclusionary rate ranging from 0% (Bernard High-Rise) to 32% (Valleymede High-Rise). **In our experience, inclusion rates over 20% are rarely financially feasible.** Furthermore, it is also atypical for a mid-rise building to support more affordable units than a high-rise in the same market area, as is the case for the Bernard MTSA.

Figure 2.8

“Maximum Inclusion Rates for Building Tenure Type 1” (Table 17 of the SHS Study)

Pro-forma Results Condominium with Affordable Ownership									
			Richmond Hill Centre	Valleymede	Valleymede	Major Mackenzie	Major Mackenzie	Bernard	Bernard
			High-Rise	High-Rise	Mid-Rise	High-Rise	Mid-Rise	High-Rise	Mid-Rise
Residual Land Value	Step 1	Estimation of Existing Site Land Value	\$17,500,000	\$11,493,000	\$4,224,000	\$14,320,000	\$5,129,000	\$22,225,000	\$7,164,000
		Price per square foot buildable	\$61.12	\$68.89	\$71.35	\$64.12	\$76.86	\$55.50	\$75.63
		Current Density (FSI)	3.5	2.5	2.5	2.5	2	4	2
		Units in Tower with Current Density	382	222	79	298	89	534	126
	Step 2	Upzoned Land Value (0% inclusion)	\$23,612,000	\$14,731,000	\$4,919,000	\$18,885,000	\$5,802,000	\$24,520,000	\$9,318,000
		Price per square foot buildable	\$44.41	\$52.56	\$64.91	\$52.85	\$62.10	\$48.99	\$65.58
		Maximum Density (FSI)	6.5	4.2	3.2	4	2.8	5	3
		Units in Tower with Maximum Density	709	373	101	476	124	667	189
	Step 3	Upzoned Land Value with Maximum Inclusion Rate (Affordable Price \$466,888)	\$19,813,000	\$13,939,000	\$4,716,000	\$15,862,000	\$5,658,000	N/A	\$8,000,000
		Price per square foot buildable	\$37.26	\$49.73	\$62.23	\$44.39	\$60.56	N/A	\$56.30
			Maximum Inclusion Rate (% of GFA that is Affordable)	30.0%	32.0%	8.0%	28.0%	11.0%	No Inclusion

Source: Table 17 of Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report prepared by SHS Consulting.

Scenario #2: Condominium Towers with Affordable Rental Units

SHS recommends a maximum inclusion—or “set aside”—rate ranging from 0% (Bernard High-Rise) to 13% (Richmond Hill Centre High-Rise), when considering condominium towers with affordable rental units specifically.

Based on our own modelling using SHS’ assumptions from their 2021 analyses, these inclusion rates were likely reasonable at the time. However, we **caution that these analyses should be revisited to consider today’s drastically different market conditions.**

Figure 2.9

“Maximum Inclusion Rates for Building Tenure Type 2” (Table 18 of the SHS Study)

			Pro-Forma Results						
			Richmond Hill Centre	Valleymede	Valleymede	Major Mackenzie	Major Mackenzie	Bernard	Bernard
			High-Rise	High-Rise	Mid-Rise	High-Rise	Mid-Rise	High-Rise	Mid-Rise
Residual Land Value	Step 1	Estimation of Existing Site Land Value	\$17,500,000	\$11,493,000	\$4,224,000	\$14,320,000	\$5,129,000	\$22,225,000	\$7,164,000
		Price per square foot buildable	\$61.12	\$68.89	\$71.35	\$64.12	\$76.86	\$55.50	\$75.63
		Current Density (FSI)	3.5	2.5	2.5	2.5	2	4	2
		Units in Tower with Current Density	382	222	79	298	89	534	126
	Step 2	Upzoned Land Value (0% inclusion)	\$23,612,000	\$14,731,000	\$4,919,000	\$18,885,000	\$5,802,000	\$24,520,000	\$9,318,000
		Price per square foot buildable	\$44.41	\$52.56	\$64.91	\$52.85	\$62.10	\$48.99	\$65.58
		Maximum Density (FSI)	6.5	4.2	3.2	4	2.8	5	3
		Units in Tower with Maximum Density	709	373	101	476	124	667	189
	Step 3	Upzoned Land Value with Maximum Inclusion Rate (Affordable rents at 100% AMR)	\$19,339,000	\$13,237,000	\$4,701,000	\$15,869,000	\$5,681,000	N/A	\$7,956,000
		Price per square foot buildable	\$36.37	\$47.23	\$62.04	\$44.41	\$60.80	N/A	\$56.00
		Maximum Inclusion Rate (% of GFA that is Affordable)	13.0%	7.0%	3.0%	10.0%	3.0%	No Inclusion	3.0%

Source: Table 18 of Sub-Report 4: Inclusionary Zoning Impact Assessment of The City of Richmond Hill Affordable Housing Strategy – Background Report prepared by SHS Consulting.

Practical Limitation: Affordable Rental Units in Condominiums

We also note that including rental units within condominium buildings can be challenging from a more practical perspective in terms of not only delivering the units to market, but also in terms of their longer-term maintenance and operation.

Specifically, condominium developers typically look to “recycle” their equity frequently (i.e., shifting the equity from one project into their next) and do not want to be tied to a project for 25 years after the condominiums are sold. Additionally, most condominium developers are not equipped to manage these units going forward, requiring some sort of partnership which can further complicate pro forma assumptions.

Scenario #3: Purpose-Built Rental Towers with Affordable Units

Rental development has been challenged to compete against condominium development across the GTA for some time. SHS acknowledged this condition in Richmond Hill.

The pro-forma results for rental developments tested demonstrate the challenges faced by developers seeking to build purpose-built rental in Richmond Hill. Under the specified market conditions, purpose-built rental prototype scenarios with additional density provided through the inclusionary zoning policy resulted in a lower land value than even the estimated existing land value at its highest and best use⁹². In all of the submarkets in Richmond Hill in this analysis, rental tenure prototypical developments were not viable under the test conditions and could not sustain any level of affordable inclusion. – Pg. 278, The City of Richmond Hill Affordable Housing Strategy – Background Report

⁹² The highest and best use of the existing land value is a condominium building.

SHS acknowledges that Inclusionary Zoning disincentivizes rental development by adding additional costs and further reducing rental developer’s ability to compete in the land market. Furthermore, SHS itemized financial incentives, which may be provided by the City to effectively promote the development of rental construction in Richmond Hill include, including:

- **Development Charge deferrals;**
- **Tax Increment Equivalent Grants (TIEG);** and,

- **Reduced parking requirements.**

As a result, SHS recommends no inclusionary rates for purpose-built rental apartment developments across all of the MTSAs and building typologies.

Parcel Professional Opinion

Overall, while we agree that the methodology relied upon by SHS was ultimately reasonable, it is our opinion that the **maximum unit set aside rate for affordable units arrived at across several of the scenarios are potentially unrealistic in today's market.** This again, necessitates updating of the pro formas in parallel with some of the potential improvements identified earlier in this review.

Key Themes

Theme #1: General Flexibility in Policy

It will be important to ensure that appropriate flexibility is built into any future IZ policy established by the City. Perhaps most importantly, it is critical to first acknowledge that the modelling employed by SHS—as well as any future update analysis—is illustrative in nature only. Given the hypothetical nature of these types of assessments for demonstrative parcels of land within each submarket, there will undoubtedly be unique development conditions, expectations and resulting land pricing for individual sites in practice versus theoretical development projects.

Although it is impossible to truly capture all the distinct conditions on each of these sites, it is nonetheless important to accommodate the range of possibilities or potential outcomes in this regard. As such, a **future policy implementation that avoids being overly prescriptive** while also maintaining sufficient protection of the underlying objectives or strategic goals of the municipalities is important.

Theme #2: Gradual Introduction

Based on the experience of other peer municipalities, it is commonplace to adopt an approach to **implementing new IZ policies gradually or “turning the taps on slow”**, so as to provide appropriate advanced warning to landowners and the development community. Although in theory—and perhaps at face value—this could delay the delivery of new affordable housing supply to the community, this could be a necessary first step to ensure the

longer-term sustainability of the new policy framework. This may also serve to avoid any unwanted immediate or short-term “shocks” in the local market area(s).

In addition to establishing a reasonable timeline for introduction of the new IZ policy, this initiative should also be accompanied by **active and regular communication, education and outreach** with the development community to ensure clarity of the intended direction and motivations of this policy, as well as the anticipated outcomes from the perspective of the City. With this type of ongoing communication and education, it is much more likely that undesirable outcomes can be mitigated or perhaps avoided altogether—particularly by reducing uncertainty and/or misinterpretation amongst the development community. As evidenced through ongoing discussion relating to the implementation of new IZ policies in other GTA jurisdictions, it will be increasingly important to be mindful of risks and unwanted consequences—such as reduced development activity and interest, or misinterpretation of policy mechanisms—by offering complete information to the development community.

Theme #3: Monitoring Framework

Consistent with the notion of a gradual introduction of new IZ policies, per above, a related and subsequent task for the City will be to **continuously monitor the market impacts of the new IZ policy and to actively adjust in response to any unwanted changes.**

This type of monitoring will also be required to simply update and reflect constant changes in a dynamic real estate market, including: evolving construction cost profiles and rates, changing revenue/demand prospects, adjustments to developer preferences, ongoing supply/demand relationships, broader macroeconomic trends, etc. Similarly, there may be a need to hear appeals or challenges to the policy in circumstances for which a reasonable agreement cannot be established between municipal authorities and local landowners/developers.

With respect to future monitoring, however, we recognize that this will be particularly challenging in an environment of limited financial and/or staff resources and potential lack of in-house subject matter expertise within the municipality. These challenges could also be further exacerbated if there is not a sufficient scale or magnitude of IZ-related development activity to justify the costs of monitoring in this manner.

One potential solution to this problem would be to **simplify the analyses prepared by SHS and effectively isolate or reduce to the model to its core principles** (i.e., a “bare bones” version of the same modelling that follows the same general RLV structure but with fewer individual assumptions or statistical elements to be updated). This may facilitate any future updates by municipal staff and/or others involved that may not be able to offer the same level of expertise as external consultants. At minimum, we encourage the municipality to monitor housing development activities in general and seek to draw connections to the effects of new policies (e.g., ongoing review and change over time of the number of new development applications, housing starts / completions, etc.).

Theme #4: Relationship with Other Strategic Objectives

In our experience, it is important to **remain mindful of the balancing act between the full range of municipal strategic outcomes and other land use planning objectives**. Even when a full range of preferred outcomes are worthy of consideration, they can—at times—end up representing competing priorities in need of reconciliation.

As it relates to development feasibility, for example, we note that projects can become challenged and overburdened by the cumulative effects of various charges, levies, or other limitations to development. That is, even if a development project shows promise from a return-on-investment perspective in isolation, feasibility can ultimately be impeded when considering other “carve-outs” for required affordable housing delivery, parkland dedication, integration of grade-related commercial spaces, heritage preservation, limitations to density / building heights, changes to building design, among a range of other more direct charges and fees associated with new development.

A balanced approach should therefore be taken with respect to municipal expectations around the combined delivery of the specific building and/or community features identified above in conjunction with IZ-related affordable housing. This tempering of expectations and prioritization of outcomes will be particularly important when evaluating implementation in weaker markets and/or in geographies where more significant set-aside rates are being considered.

Although there is no clear-cut solution to these challenges, we recommend that the City seek to rank-order relevant city-building objectives in terms of relative priority. The City should also be mindful of the fact that most development projects are not capable of supporting a significant proportion of uses that do not contribute directly—or meaningfully—to revenues.

3.0

Conclusions

Based on our review of the IZ Impact Assessment prepared by SHS and in light of the evolving legislative context in which new IZ policies must now be implemented, it is our opinion that selected updates are required to further bolster the financial feasibility testing prepared on behalf of the City of Richmond Hill.

The following provides a summary of our more specific findings in this regard:

- Overall, we believe that the RLV approach and analytical structure adopted by SHS represents a **reasonable and reliable methodology** for understanding the high-level implication of implementing IZ in Richmond Hill. This underlying structure appears to be consistent and appropriate with the fundamental intent behind *Ontario Regulation 232/18*, as originally worded in 2021.
- Although we cannot necessarily guarantee the full accuracy and completeness of the various pro formas prepared by SHS, we are **sufficiently confident that the RLV approach and analysis described above has been applied correctly**. We have also, however, recommended that some specific assumptions be revisited and/or updated to reflect more market data that are now available, as well as to provide what we believe to be a more realistic “picture” of feasibility conditions in today’s market.
- The various statistical inputs and other assumptions requiring professional judgement relied upon by SHS as part of their analysis appear to be mostly reasonable and consistent with our own research and experience in this market area. That said, we **recommend the following assumptions be revisited**:
 - Pre-Construction and Construction Timing
 - Above and Below Grade Hard Costs
 - Financing Rates
 - Application of Discount Rates
- Beyond the selected updates identified above, **no fundamental deficiencies nor other material issues were identified** as part of our review, which need to be addressed as part the reporting prepared by SHS to date.

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