Implementing Inclusionary Policy to Facilitate Affordable Housing Development in Ontario

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1. Introduction

Urban planning is about anticipating requirements for urban activities and setting in place policies and plans to accommodate these activities in an orderly, efficient, sustainable and just manner. It also seeks to facilitate orderly and efficient installation of necessary infrastructure development. Planning works in conjunction with the market to allocate land and specify the use of land in a way that includes a wide spectrum of anticipated future need and requirements for a healthy vibrant community, neighbourhood, town or city.

To the extent that certain segments of the population have less capacity to function in the market (they lack what economists call “effective demand”) usually because they have low income and low influence on the political process, they are restricted in accessing land and services. They cannot compete with other potential users that have higher capacity to pay. Planning seeks to ensure opportunity and availability of housing and services for these households.

At the same time, the opposition of existing residents to the development of affordable rental as well as multi unit apartments (higher density than already exists) as infill in existing areas represents a challenge for planners seeking to address affordable housing needs.

To the extent that both market economics and resident opposition preclude opportunities to provide affordable housing, but all communities have a range of incomes and need for a range of affordable housing opportunities good planning principles suggest that it may be appropriate to establish, by regulation, some degree of inclusion.

This report was commissioned by the Ontario Non-Profit Housing Association (ONPHA) to examine the potential to strengthen legislation to encourage and enable municipalities adopt inclusionary policies, specifically to encourage production of affordable housing in Ontario and to develop specific recommendations in this regard to the Province of Ontario.

ONPHA is interested in this regulatory approach as a way to enhance provision of affordable housing. The association is also concerned about resistance for the development of non-profit affordable housing and the NIMBY reaction that often confronts non-profit corporations seeking to supply affordable and supportive housing. An inclusionary requirement can be an effective way to combat NIMBY as well as addressing concerns about creating concentrations of poor households since inclusionary approaches help to disperse lower income households across neighbourhoods that include a broader mix of incomes.
The report commences with a brief review of recent experience regarding the provision of affordable housing through the planning process, which has been expanding in other jurisdictions. It then reviews the rationale and arguments for and against this policy tool. The key issue of economic feasibility is investigated and recommendations then developed with a view to balancing public objectives of inclusion and affordability against the rights and incentives for private landowners and developers to realize a fair profit.

The key challenge is to balance the share of gain between the public approval authority and the landowner, such that the requirement to meet certain obligations does not impose a “tax” on development or cause development to be uneconomic.

Clarifying Terminology

In this paper we explore the concept of inclusionary policies for affordable housing. This refers to a policy that obliges, or encourages developers to include some portion of the dwellings at a prescribed price level deemed to be more affordable than might otherwise be constructed.

The specific term “Inclusionary Zoning” is commonly used in the US to refer to mandatory zoning requirements to provide affordable housing. Here we use the more general term inclusionary policies to distinguish from the specific US models and to reflect a broader set of options.

As discussed in section 2.2, inclusionary polices may be mandatory and applied to all development, or voluntary.

Typically, mandatory approaches include "offsets" to compensate developers for the cost of providing units at lower values.

In the case of voluntary inclusion, this is premised on offering a benefit as an incentive to encourage the developers to include affordable units.

The paper makes reference to Sec 37 of the Ontario Planning Act which is a provision that enables municipalities to authorize increases in height or density than otherwise permitted in the zoning bylaw in return for the provision of “facilities, services or matters” set out in the bylaw. The argument is made that as currently drafted, Sec 37 does it necessarily provide sufficient authority to municipalities to be used as a way to seek inclusion of affordable housing as a condition of development approval and that affordable housing is just one of a number of “facilities, services or matters” that can be provided in return for the increase in density.
2. Affordable Housing Inclusionary Policies: Background and Experience in other Jurisdictions

Inclusionary policy refers to local municipal zoning bylaws, ordinances or policies that require or encourage the production of affordable housing as part of development approval process for market housing. As discussed in more detail below, the term inclusionary zoning is frequently used in the US and is one specific form of inclusionary policy. This brief includes these as well as other forms of inclusion, as implemented in the UK and in a few Canadian jurisdictions.

When the concept was first introduced it mostly referred to mandatory zoning obligations with no compensation. However, over time the concept has evolved to include a broad spectrum of possibilities including: mandatory requirements for affordable housing, coupled, in most cases, with offsets against the cost of providing the affordable housing, incentive based zoning that is voluntary, but results in the production of affordable housing if the incentives are taken up; and negotiated development approvals that either set land aside for non-market development or produce affordable housing based on a policy framework articulated in local plans.

**US Experience**

As a precursor to the enactment of inclusionary zoning ordinances in many jurisdictions an important contextual feature in the US has been the legal challenge from affordable housing activists, against exclusionary and discriminatory practices. This has resulted in affirmative action fair share legislation in a number of States (most notably New Jersey) which establish an enabling framework for municipal zoning ordinances.

The concept first emerged in the US in 1971 in Fairfax County, Virginia which passed a mandatory zoning ordinance that required developers of more than 50 units of multi family housing to include at least 15% of the dwellings within an affordable range that was defined as addressing the housing needs of households between the 60th and 80th percentile of median household income. This ordinance was subsequently struck down by the Virginia Supreme Court as constituting a “taking”. This was a critically important decision and set the stage for subsequent efforts which took great care to balance inclusion requirements with specific compensating cost offsets so that the “takeings” challenge could be avoided.

In nearby Montgomery County, Maryland a similar ordinance (Moderately Priced Development Unit – MPDU) was passed in 1973, and has survived to this day, with some refinements and improvements. In exchange for a density bonus of 20%, this ordinance requires all developers in the County of more than 50 units to set aside 12.5 % to 15 % of their units as “moderately priced dwelling units”. This program has produced
more moderately priced housing units than any single government in the US and is considered the most successful example of an inclusionary zoning program at the county level in the US. Montgomery County’s MPDU law has produced more than 10,000 affordable housing units over 20 years—and has never been challenged legally [Tustian 2000].

Inclusionary zoning is now a major feature of zoning ordinances across the US. It has been introduced in many municipalities in a large number of States across the country. In some cases these ordinances are State mandated programs which obligate local governments to address affordable housing provision through the development approval process. The most well known of these is the program introduced in New Jersey in 1983 through a New Jersey Supreme Court decision that required local governments to use “affirmative governmental devices...including...mandatory set asides” to achieve fair-share housing plans. Since this time inclusionary zoning has become a major feature of all local government fair-share housing programs at the local level in New Jersey.

Stimulated initially by the proactive efforts of cities such as San Francisco, over the years California has also taken a lead role in developing a model ordinance to assist municipalities towards adopting inclusionary zoning ordinances and is now considered one of the leading States where inclusionary zoning has been implemented locally. The California General Plan Law requires that all localities adopt a General Plan and the Housing component of the plan be certified by the Department of Housing and Community Development. In 1980 the requirements related to the “housing element” of general plans were strengthened and interpreted by the Department of Housing and Community Development as obligating local governments to “zone affirmatively for regional housing needs”. The Department prepared a Model Inclusionary Zoning Ordinance that they provided to local governments as an essential tool to achieve affordable housing goals. [NHC 2004]

This advocacy stance has shifted over the years in California to reflect the changing priorities of successive State governments, ranging from a “hands off” approach towards outright. However, in 2001, the case of Home Builders association vs. the City of Napa established that inclusionary zoning is a constitutionally valid extension of a local jurisdiction’s zoning powers. As a result of the evolution of inclusionary zoning authority in California, by March 2003, one fifth of all localities in the State were using inclusionary zoning more than 107 jurisdictions) including San Francisco and San Diego. In a survey of jurisdictions one third of those reporting using inclusionary zoning reported a total of 34,000 affordable dwellings produced [NHC 2004].

An important feature of inclusionary practice in the US is that many of the participating jurisdictions involve development of single family subdivisions. Because this is the predominant form of housing development, and is captured in these inclusionary requirements the outcome in the US tends to be on affordable homes for purchase by moderate income first time buyers. As discussed later, the economic feasibility is more
realistic with a target of marginal buyers compared to generating product targeted to very low income households. This is very relevant to Canada where the vast majority of newly constructed housing is similarly detached and semi-detached homes for sale often in the suburban growth areas of metropolitan regions.

**Canadian Experience**

The Canadian experience with inclusionary type policies is limited to Ontario and British Columbia; in both instances the approaches have been mostly based on achieving affordable housing contributions through incentive based negotiated approvals, rather than the US style mandated programs.

For example, since 1988 the City of Vancouver has required that the post Expo development of False Creek include 20% social housing. This approach has yielded an affordable housing requirement for the False Creek area of 1,704 units. In nearby Burnaby there has been a requirement that on municipally owned land at least 20% of the development represent affordable housing development. It is important to note that these requirement simply obligate the land owner to set aside sites for non-market development, but still depend on public subsidy programs to build the units (albeit with no land cost).

The City of Vancouver has also pursued affordable housing contributions through density bonusing and “comprehensive development zones’ where contributions towards affordable housing are negotiated in the context of swapping bits of City streets and other land parcels.

In 1993 the Municipal Act was amended in BC enabling local governments to undertake “comprehensive development zoning” which includes the provision for some form of incentive based inclusionary policy for large projects where density bonuses are negotiated. Many municipalities in British Columbia are using these powers to achieve affordable housing contributions.

In Ontario the closest recent example to an inclusionary approach was the 1989 “Land Use Planning for Housing” policy statement (PPS) which encouraged municipalities across the province to achieve 25% of affordable housing in newly developing areas. This was replaced by a more vaguely worded statement in 1996 with no numerical targets. The PPS was again amended in 2005 with the current policy stating that it is Provincial Policy that planning authorities “shall provide for an appropriate range of housing types and densities to meet projected requirements of current and future residents...by: establishing and implementing minimum targets for the provision of housing that is affordable to low and moderate income households”. In response to the 1989 housing policy statement, many municipalities including Ottawa-Carleton, Toronto, Hamilton-Wentworth, Niagara, London and Peterborough included specific targets for housing affordability in their official plans.
In 1991, the City of Toronto and the Ontario Ministry of Housing initiated a study on the feasibility of introducing mandated inclusionary zoning for the City of Toronto and by extension the province of Ontario. Although the authors of the study calculated that a mandatory approach would produce a significant contribution towards achieving the City’s affordable housing objectives and that a modest 5-10% requirement for affordable housing would not distort development economics, it was noted that mandatory inclusionary zoning could only be introduced through increased powers from the Province. Subsequent analysis led to the conclusion that a negotiated approach involving incentives represented a preferred course of action.

The new Toronto Official Plan contains general policies regarding the use of Section 37 (bonusing) of the Planning Act for affordable housing as well as a policy that applies to sites over 5 hectares where height and density increases have been negotiated. This policy requires a 20% affordable housing contribution.

In 2004 the City of Langford on Vancouver Island adopted an “affordable housing program” which appears on the surface to represent the closest approximation to a consistent application of an incentive based inclusionary zoning approach in Canada. The program requires that all developments involving rezoning of 10 or more units provide 10% of the housing as affordable housing which are marketed to first time buyers with low household incomes and are subject to affordability housing agreements, restricting re-sales and registered on title.

The Ville de Montreal has also created a framework to encourage the development of affordable housing with a two tier approach: publicly funded deep subsidy affordability and low end of market unsubsidized affordability. The latter embraces an inclusionary objective but the city’s policy document makes an explicit distinction between an incentive-based and mandatory mechanism. Because Quebec municipal law does not allow for the (US style) mandatory inclusion of affordable housing, the city of Montréal’s approach has therefore been to create incentive-based programs, aiming to maximize its

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1 Section 37 of the Ontario Planning Act allows municipal councils to authorize increases in height and/or density over the prescribed amounts stipulated in their zoning bylaws in return for facilities, services or matters as set out in the by-law. The provisions of this Section also authorize municipalities to secure the services, facilities or matters through contractual agreements with developers. Affordable housing can be considered as a “service, facility or matter” for the purposes of the bylaw. However, affordable housing often competes with other matters that may have higher priority in the minds of Council and for this reason, Section 37 has not often been successfully employed to secure affordable housing. In this paper we suggest that the Province could strengthen municipal authority to use section 37 for affordable housing by specifically referencing affordable housing as one of the “services, facilities or matters”. And by stating that municipalities are expected to secure affordable housing in pursuit of the Provincial interest under the provisions of Section 37.
capability to intervene while working within the powers it has under current legislation. Montréal has identified two specific targets in the inclusionary strategy:

- that 15% of new housing units built in Montréal be social or community housing – targeted to households with low or very low incomes, generally below $35,000 household income; and

- that another 15% of new housing units be affordable and built by the private sector (rental or affordable home ownership). Here the target group is moderate income roughly $35,000 to $55,000. Some modest financial assistance can be made available along with density bonusing.

An evaluation of the cities policies after only two years since implementation in 2004 found that with this voluntary approach the city has surpassed its goal – 39% of new housing constructed in Montreal has meet the affordability targets, both in the very low and modest income categories.  

**UK Experience**

In the UK most development is subject to “planning permissions” which are negotiated with local authorities. These planning permissions are generally premised on securing contributions towards the specific costs that are directly associated with development impacts (much like development charges in Ontario), referred to as “planning gain” and secured through agreements under section 106 of the 1990 Town and Country Planning Act. Policies dating back to 1981 enable affordable housing to be secured on all larger housing developments requiring planning permissions including requiring private developers to meet the need for affordable housing, provided that the local authority has adopted general development plans that identify the need for affordable housing.

Recent changes to government policy have reduced the size thresholds above which contributions would be sought in most circumstances (for example “rural exception sites” with less than 6 units are exempted) as well as linking it to other government policies on social inclusion, creating mixed communities and achieving an “urban renaissance”. Most significantly, in 2000, the government amended its policy to make it clear that refusal to contribute towards affordable housing constituted a legitimate basis,

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2 While referred to as voluntary and incentive based, in Montreal the opportunity to seek inclusion arises in almost all major redevelopment projects as in Montreal this typically involves rezoning from industrial brownfield sites. Thus it is a negotiated process, much like Sec 37 in Ontario. However, unlike Ontario there is not a culture of reaction and appeal to a quasi judicial body (although one does exist). In most cases inclusion is negotiated in exchange for densities that allow the inclusionary requirement to be achieved without unreasonably impacting developer.

3 The criteria for affordable homeownership in 2006 was price under $145,000 for singles and $175,000 for families
in and of itself, to refuse planning permission. Recent changes propose to widen the scope of the policy to include small sites and commercial developments as well as replacing negotiated contributions with standard financial contributions to be used primarily for on-site provision.

Recent estimates are that between 10,000 and 15,000 units of affordable housing have been secured annually in England through the use of this mechanism.

The section 106 approach to affordable housing provision in the UK starts with the premise that the land use planning system through the approvals process determines the number and allocation of new housing units as well as their physical attributes. The inclusion of affordable housing as part of the approval process is intended to ensure that a proportion of these units, based on local need, are affordable through land and financial contributions. Developers are therefore involved in contributing towards affordable housing as part of the allocation of “planning gain‘ that is generated through the granting of development permissions.

It should be noted that in most cases, this only requires the developer to set aside land on which units can be constructed with capital subsidy under the national social housing program. The developer is not obligated to build the units at his cost with no subsidy. In some cases the developer will construct the units and turn them over to a registered social landlord, in other cases the RSL will take the land and manage the construction independently. However, in some cases the affordable units are targeted to first time buyers and the developer will build and recover costs through sales at these unsubsidized entry level prices.

2.1. Reasons for Introducing Inclusionary Policies

For the most part, the primary reason for the introduction of inclusionary zoning programs has been the high cost of housing and growing concerns about affordability – not just for the poorest households but also the middle class service workers – like nurses, teachers, and firemen.

In North America housing costs began to spiral upward in the 1970’s and have continued rising virtually unabated since then. In light of these increases the need for affordable housing has grown. In addition to poor households, increasing housing costs are affecting even moderate income households in many jurisdictions. In many cities employers are finding it increasingly difficult to recruit workers because of high housing costs and are asking local governments to help respond.

At the same time funding from senior levels of government for housing in the US has fallen to an all time low [Zeigler, 2002]. In the US, State funding for housing has not been able to address the shortfall in Federal funding; in fact, many States are facing severe budget crises in response to cutbacks to Federal grants for a wide variety of programs.
With limited local funds available to address housing affordability, zoning for affordability has become an attractive option.

Inclusionary zoning is seen as a potential way to respond to these concerns and is seen to have two laudable goals: to create more affordable opportunities: and to integrate affordable units throughout a jurisdiction (avoid concentrations of poverty and exclusion) [Tustian, 2000].

A similar contextual situation regarding housing affordability exists in Ontario. Here the housing affordability crisis arising from high housing costs has been exacerbated by the total withdrawal by senior governments from affordable housing programs in 1994 and their slow and limited return commencing in 2002. A well structured, flexible and realistic inclusionary zoning program could represent part of a coordinated response towards addressing affordable housing needs here.

In addition to addressing the need for affordable housing, the attractive features of introducing inclusionary zoning for use by local governments in Ontario include the following:

- There is little or no financial cost to local governments. Various studies in the US have concluded that the cost of providing affordable housing under an inclusionary zoning program is spread to varying degrees amongst land owners (through a reduced land cost), developers, purchasers of market units (generally very low impacts) and, if incentives such as density bonuses are offered, by the community at large.4

- Providing for the creation of income integrated communities rather than isolating affordable housing in separate enclaves within cities.

- Addressing sprawl since affordable units are generally denser that typical suburban housing. This was an unexpected benefit of the 1989 Ontario Land Use Planning for Housing policy statement. By introducing policies in Official Plans to achieve 25% affordable housing, which was often defined as smaller lots/units, suburban municipalities were able to increase overall densities resulting in more compact communities.

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4 While it is theoretically possible to achieve with limited cost to government, this reflects approaches where the affordable units target marginal buyers and provide a relatively more affordable ownership option, paid for by consumer; where deeper affordability is desired, approaches typically involve direct subsidy with a non-profit or local housing authority purchasing units “at the affordable threshold price” for use in a non-profit rental portfolio (with scattered sites).
2.2. The Elements of Inclusionary Zoning

**Mandatory or Voluntary Approach**

The survey of US examples of inclusionary zoning programs reveals a variety of approaches although these are essentially variants around two primary features:

- Mandated programs that require all residential developments over a certain size to include a percentage of affordable housing and include specific offsets or compensation for the developer (this approach is used in New Jersey).

- Voluntary programs that establish a schedule of incentives which developers may elect to negotiate in exchange for inclusion of some negotiable level of affordable dwellings

A variant on these US approaches which is worthy on consideration in Ontario is:

- A mandatory mechanism that is trigged only if a developer seeks a rezoning or subdivision approval. The developer is able to build as of right under current zoning, but if he elects to seek higher density or other zoning amendments the requirement to include affordable housing would be triggered. In the context of prevailing smart growth and intensification policies in Ontario, it is anticipated that the vast majority of new development in larger municipalities will involve rezoning (and in greenfields sub-division approval) so this is effectively mandatory, but provides a developer the prospect of opting out.

A fourth option is that used in Vancouver and other jurisdictions – requiring land to be set aside for non-market housing but with no obligation on the developer to build these units, unless appropriate subsidies are provided. This may produce some affordable housing but is less effective in achieving the mixed income that is implicit in inclusionary policies.

**Threshold (Size of development, new construction, reuse)**

The threshold for size of development at which the inclusionary requirement kicks in to cover a broad range. Most often for new development the threshold kicks in at 10 units or more, although in certain denser downtown districts, where multi unit developments prevail, the threshold is much higher to reflect the size of development that would generate a stand alone affordable housing component that could be marketed separately (for example in Vancouver the threshold is 240 units).

In some jurisdictions developments that propose to reuse existing buildings are exempt, while in others the obligation kicks in at a certain threshold (in Burlington, Vermont the threshold for new development is 5 units, while for adaptive re-use it is 10 units).
Ottawa and Toronto have applied the provision to large sites through their Official Plan policies, i.e. any site exceeding 2 or 5 hectares, respectively.

**Definition of Affordability (ownership and rental)**

Municipalities in the US define affordability for the purposes of the program in various ways, mostly relating to percentiles of median household incomes related to household size. In most municipalities the target income groups are higher for affordable ownership housing than for rental housing. In some cases affordable ownership housing is targeted towards households at between 80% and 120% of the median household income, adjusted for household size (in Burlington Vermont this figure is 75%). Typically when rental housing is identified the target is usually 50%-80% of median family income.

While a percentage of area family median income is a common feature across many housing programs in the US, this has not typically been the case in Canada. In social housing programs, Canada has defined a set of core need income thresholds (CNIT), which is now revised and renamed as Housing Income Limits (HILs), both as program eligibility criteria and as a basis to measure the number of households in need. Unlike the US system which are income based and thus reflect ability to pay, the CNIT/HILs are derived and are rent based, premised on the income required to afford an appropriately sized unit (relative to household size and composition) without spending more than 30% of gross income.

One consideration in an income based versus rent based benchmark is data availability. In Canada the rent data are more frequent available via the CMHC annual (now again semi annual) rent survey; income data at the local level are not as readily available so there are gaps and lags between the census dates. Most recent programs in Canada have defined affordability in relation to the average market rent or a percentage thereof (e.g. since implementing federal/provincially funded affordable housing programs some municipal jurisdictions or provinces have specified that a certain proportion of funded units achieve rents set at 70% to 80% of the CHHC average market level for that unit size.

There are, in addition, requirements relating to those eligible to apply for the housing that is created through these programs. These include:

- For rental housing, households on the municipal waiting list for affordable housing.
- For ownership housing, first time buyers as well as meeting the affordability criteria.

Clearly the benchmark of affordability defines the rent or purchase price that will be generated and the differential over market values. Deep targeting is problematic in an inclusionary program without some form of subsidy incentive – the reduced land value
and additional market profit margins generated by density bonusing will seldom, if ever facilitate affordability at the very low income levels.

**Defining the Extent of Obligation (Percentage of units to be included as affordable)**

In many (US) jurisdictions municipalities require 15% of all units to be affordable; some go as low as 10% and others go as high as 25%. In some municipalities there are different percentages for different districts to reflect different planning priorities.

In Canada, for the Toronto waterfront the proposed obligation to developers is 20% to be secured through a Section 37, although developers have the option of providing the units off site, or providing the land or cash equivalent. The affected developers have appealed this policy to the Ontario Municipal Board. The matter remains unresolved, as of the time of writing this report Agreement. The City of Vancouver also requires that sites to accommodate 20% of units in False Creek be set aside for “non-market” development (with proviso that a provincial program will help subsidize development).

In Ottawa, the City included affordability objectives in the Official Plan, as a voluntary requirement, premised on 25% of rental units to be affordable (at 30% of income) to households with incomes at the 30th percentile of the household income distribution; and for ownership housing to be affordable to the 40th percentile of the household income distribution. This was appealed by a number of builders as well as the Ottawa Homebuilders Association. The objections specifically claimed that this requirement was not feasible and would be unmarketable.

**Ensuring Affordability over the Long Term**

Municipalities with inclusionary zoning provisions often require that affordability be secured over the long term. For rental housing these are fairly straightforward and are generally based on project specific agreements regarding affordable rent levels that are timed to terms of 10 to 35 years. Alternatively, the approach used in Maryland and emulated in other jurisdictions requires the developer to sell a proportion of the designated units at the affordable threshold price to the local housing authority which then operates these as part of its rental portfolio.

For ownership housing preservation of affordability is generally more complex, but often involves registration of controls on resales on title, providing the right of first refusal to a housing trust or non-profit agency and restricting the price increase on resale to a certain amount. An interesting variation on this is being explored by developers and the Toronto Community Housing Corporation to provide second mortgages to purchasers and share the appreciation in value in proportion to the mortgage share, as well as requiring the right of first refusal to a housing trust.
Defining the Extent of Incentives

The US literature and experience has demonstrated that a variety of approaches are possible to offset the inclusionary requirement and create a financial incentive to the developer. Developer incentives include the following:

- Subsidies;
- Fee reduction;
- Fee deferral;
- Fee waiver;
- Property tax abatement;
- Design flexibility;
- Fast track processing;
- Density bonuses.

In the US, density bonuses are by far the most extensively used incentive. These can range from between 10 and 25 percent in Burlington Vermont to as high as 4 sq ft of market housing for every 1 sq ft of affordable housing in downtown Chicago. In California more than 90% of municipalities that have inclusionary zoning policies provide density bonuses.

The recent federal-provincial affordable housing program (variously labelled the CRSP, Strong Starts and now DOOR, in Ontario) has used direct subsidy to procure affordable units (meeting the benchmark of average market rent, and in a number of jurisdictions private sector proponents have participated in the program, suggested that there is a willingness of private developers to build affordable and mixed income projects. These typically involved a combination of capital grant, waived fees and charges and reduced property tax rates. In the Region of Waterloo the average grant per unit for private proponents was just under $25,000 on units with an average capital cost of $75,000 (so grant equals 35% of capital cost, which is not necessarily market value).

Deferral or waiving of fee and development charges generates specific cash reductions in property development costs and are explicit values that can be identified and modeled.

Streamlining the development process is theoretically possible to quantify, but very difficult to do so – if depends on how much the developer has spent, the proportion which is covered in interim construction financing and the developers requirement for return on equity, for example if he already owns the land versus acquiring specifically for the project and financing.
Design flexibility provides the developer with options to be creative in minimizing the cost impact of inclusion, while balancing the marketability of the market units. It is not so much a quantifiable benefit as a useful one to secure greater willingness for developer to participate.

**Guidelines on size and distribution of affordable units**

Most US ordinances do not require the affordable/modest units and market units to be identical; however they generally encourage design that makes the affordable units appear similar in outward appearance. There is also a general practice of disbursing the affordable units through a development rather than massing all in one part of the site – which enhances the objective of inclusion.

**Alternatives to on-site construction**

The most common alternatives to on site construction are:

- The provision of land;
- Payments in lieu of construction (generally priced higher than the cost of developing affordable housing);
- Options for off site construction of the affordable housing (i.e. providing land or units for affordable housing on another site owned by the same developer, with the original site developed for market housing).

The alternative provisions are generally structured to encourage on site provision of affordable housing, so there is a cost premium associated with not providing the housing on site. The offsite option is often criticised as not facilitating the objective of inclusive mixed communities.

### 2.3 Barriers to Introducing Inclusionary Zoning in Ontario

**Legal Barriers**

There exists a body of legal opinion that inclusionary zoning for affordable housing could not be successfully introduced under present circumstances in Ontario based on a legal precedent from 1979 which prohibited municipalities, under the (then) current Planning Act, from using zoning powers to regulate users of buildings (as compared to the use of the building). The case known as Bell vs. the Queen dealt with an attempt by the then Borough of North York to restrict the use of single family dwellings to no more than 2 unrelated persons. The court ruled that the legislature had not intended to grant
the authority to impose such a restriction by municipalities when it enacted the Planning Act.

Although this particular case does not reference affordable housing, the legal experts who have examined the constraints on powers granted to municipalities under the Planning Act have concluded that the restrictions on regulating users would extend to instances where zoning requires affordable housing to be provided since affordability relates the use to the user (i.e. affordable housing is intended for those who cannot afford market housing).

It is important to note that this opinion has not been tested in the courts. In fact, the Ontario Human Rights Code, which in Part I provides for broad freedom from discrimination, under Section 13(1) clarifies that “a right under Section I is not infringed by the implementation of a special program designed to relieve hardship and economic disadvantage or to assist disadvantaged persons or groups to achieve equal opportunity…” Whether a municipality can successfully argue that this provision could be extended to municipal bylaws addressing affordable housing in order to achieve “equal opportunity” is unclear.

No such restrictions on municipal authority appear to exist under US law where, as described earlier, the courts have ruled in favour of inclusionary zoning programs in a number of instances. In this respect, the American constitutional and jurisdictional landscape differs from the Canadian context, particularly with reference to obligations by governments to address racial and economic factors when dealing with housing.

In any case, these are legal matters that would be best addressed by legal experts. It therefore may be worthwhile to ask a panel of legal experts to examine this issue further. This type of legal analysis is particularly relevant at this point in time since the Province has recently amended Section 34 of the Planning Act to grant municipalities the power to zone with “conditions” – Section 34(16). These changes came into force on January 1, 2007 and potentially imply a mandatory form of inclusion. It would worthwhile to clarify whether “zoning with conditions” could include a condition that affordable housing be included in development.

Even if it is accepted that inclusionary zoning for affordable housing cannot be introduced by municipalities under the current Planning Act, it is possible for the legislature to amend the Act to explicitly provide for this authority, particularly since the Ontario Human Rights Code already provides a context for this type of approach. The exact format of these amendments may differ depending on whether the approach leans towards a mandatory requirement or is more incentive based. As discussed later in this paper, economic analysis suggests that incentives, particularly density based incentives, could make the provision of affordable housing within private developments profitable for developers, particularly if targeted towards affordable ownership.
A stronger policy directive from the Province may be necessary to encourage municipalities to achieve affordable housing initiatives with private sector participation across the Province. As mentioned previously, the Province has already included a provision in the Provincial Policy Statement, 2005 that planning authorities establish and implement minimum targets for the provision of housing which is affordable for low and moderate income households. Since municipal council and OMB decisions must be consistent with the Provincial Policy Statement, this statement could be further strengthened to clarify that municipalities either can, or are expected to, use their land use regulatory powers to help achieve their minimum affordable housing targets.

The Province could also clarify in Section 2 of the Planning Act (Provincial Interest) that the “adequate provision of a full range of housing” includes particularly the provision of affordable housing and that this is necessary to address the provincial interest. Other amendments to the Planning Act may include:

- Amendments to Section 51(23) and (24) regarding Plans of Subdivision to clarify that the provision of affordable housing is one of the criteria that should be considered in the subdivision process and that the provision of affordable housing could be included as a condition of subdivision approval.

- Amendments to Section 34(16) to clarify that a condition of zoning may include the condition of providing affordable housing.

- Amendments to Section 37, regarding the use of bonusing to clarify that the provision of affordable housing is one of the “facilities, services or matters” that may be required by a municipality in return for increases in height or density of development and that such provision can be secured by way of an agreement.

These matters will be explored further in the concluding section of this paper.

**Impact on the Cost of Market Housing Units**

A frequent argument against inclusionary zoning is that it would increase the cost of units not those prescribed as affordable housing.

Basic economic theory asserts that ANY form of regulation will tend to constrain supply and therefore will impact on the market clearing price (move supply curve to the left). So from a purely theoretical perspective this argument is not without basis. However it is an indirect effect. House prices are set in the market, they are not cost based, so the developer has limited potential to shift costs sideways – except in a rising market where there is already tolerance for price increases. In a stable or stagnant market, the developer will determine if he can absorb the impact and may elect not to build, reducing supply, which in turn can impact price, as indicated above. This risk is however removed if the inclusionary policy is designed with a fair level of offset
(effectively making the impact of inclusion cost neutral, or ideally leaving a modest incentive, as is the case in Maryland)

Empirical work undertaken in the US concludes that the cost of impact fees (which can be related to the inclusionary requirement for affordable housing), is largely borne through decreases in the selling price of land, although in some cases may also include a small increase in the purchase price of market units (see NHC, February 2004). We reach a similar conclusion in the section on the economic feasibility of affordable housing of this paper.

A study by Malone Given Parsons that was prepared for the Ministry of Housing in the early 1990’s on the implications of introducing a mandatory inclusionary zoning regime in Ontario concluded that a modest (5 to 10 percent) affordable housing requirement would have little appreciable impact on the housing market.

Further studies carried out in the US suggest that “cost offsets” and incentives such as density bonuses, can under many market conditions, compensate the developer for the cost of building the affordable units (NHC 2004). Our section on economic feasibility reaches a similar conclusion. In the case of these types of incentives, the cost can be seen as being borne by the community at large (for example, by having to accommodate additional growth where there is a density incentive provided).

**The Development Industry Will Oppose Inclusionary Zoning**

Whatever the economic evidence, the development industry is not likely to willingly accept mandatory inclusionary zoning (i.e. without some form of offset). The development industry has stated on many occasions that they are interested in a planning regime which is characterized by certainty, or more correctly they do not like a regime with uncertainty. There is an interesting contrast between the US approaches and those in the UK. In the US most inclusionary zoning ordinances, while leaving some flexibility for the developer to creatively meet the performance requirement do prescribe a specific set of requirements and associated offsets The UK (sec 106 process is a complex negotiated process and in a recent major inquiry was identified as a serious impediment in the supply and price of new housing (Barker Review). The lesson for any approach in Canada is that any requirements should be clearly framed, both with respect to the developer’s obligations as well as those of the municipality.

More often than not, and especially in larger metropolitan areas, developers apply for additional density than that permitted under zoning legislation or contemplated through official plans. An incentive based inclusionary zoning system that is intended to achieve a number of public objectives, and offers additional density while establishing a level playing field for all, will clearly be met with greater acceptance than a mandatory system with no incentive package, particularly if presented with the economic feasibility analysis presented later in this paper.
Density Incentives to Achieve Affordable Housing Distort a Planning System that is Premised on Optimal Physical Form

Over the years, evidence has shown that developers will apply for increases in density as a matter of course, whatever the planning regime (whether based on floor space index provisions or whether based on height and form). These can frequently be justified on “planning” grounds. A number of OMB decisions suggest that, more often than not, it is possible to justify density and/or height increases as “good planning”, whatever they are (see for example OMB Decision 2532 PL060524 re 371, 373-377 and 379 King Street West). In other words, achieving “optimal physical form” appears to be subject to somewhat arbitrary judgements.

The premise of incentive based inclusionary zoning is that a bonus density regime should be used to achieve affordable housing which represents a necessary public good that is directly tied to the provision of market housing. The key to making it work in Ontario is to establish a planning framework whereby the rules for an incentive based system of inclusionary zoning are similar in all local jurisdictions and where the Provincial expectation is made clear that incentives should be used to achieve affordable housing through the development process. This will be discussed further in the concluding section of this paper.

3. The Economic Feasibility of Inclusionary Zoning

Much of the extensive US experience has evolved in a legal context that prohibits “taking” and intrusion of property rights (contested under constitutional rights). As a result, the more than three decades of experimentation and withstanding legal challenges have underpinned a system that many argue effectively balances public with private interests. Any effort to implement inclusionary zoning in Canada should build on this experience.

Understanding the financial impacts of inclusion

Land has no inherent value, it is the potential to put that land into productive use and the revenues that such production can generate that creates a value. So a forested property may be valued based on potential to extract lumber; farmland values will be based of crop production; and residential property will be valued based on the sales value of units produced (or in case of rental the capitalized value of the net income stream from rents).

In most cases land use is regulated – so in case of a forest, a timber license is required, in urban land, planning and development approval is necessary. Where the use can be
enhanced (to be more productive, the approval process intervenes to ensure that this is not excessive (e.g. compatible with adjoining uses and not noxious).

The permissible use of property (usually defined by a zoning or land use bylaw) provides a guideline on its potential use and values will be accordingly derived.

Granting authority to increase the quantity of use and related revenues translates into higher value. Purchasers of property may have grounds to believe that they can present an argument to the planning authority to increase productive use (e.g. higher value product or more units reflecting increased allowable density) and accordingly in anticipation may be willing to offer a higher asking price than the current designation would suggest. It is the public authority to control use – and authority to increase the productive capacity of land that enhances value. The argument is therefore made that increased values derive from the public approval process so there should be a public (community) sharing or the enhanced value. Thus, in the UK inclusionary zoning is tied to a system that is labelled “planning gain”

Land values are typically based on a residual value. This approach calculates the potential revenues from use or development, subtracts all costs related to development and the remainder (residual) is deemed to be a fair reflection of market value. This approach is used here.

A simple case study, presented in Exhibit 1, helps to illustrate the basic premise of land valuation, inclusionary zoning and how the financial penalty imposed on the developer can be offset. Since density bonusing is by far the most frequent form of compensation, this approach is used here.

The base case is a medium sized property (200 x 240 ft with a gross area of 48,000 sq ft). It is assumed that current zoning would permit development of 50 units (gross size of 1,000 sq ft each) with an anticipated market value of $300,000. The target price for the inclusionary affordable units is $150,000 (the definition of affordable and variations thereof is discussed later). Notwithstanding the price difference between market and affordable in this simplified illustration, it is assumed that all units (market and affordable inclusionary units are identical in size and cost (an assumption that is later relaxed in Case D).

In the base case, the expected market value is $15 million; hard and soft costs, including developer profit at 15% of market value, total $13.5 million, leaving a residual land value of $1.5 million ($31.25 per sq ft of land). This is the amount a rational investor/developer would offer for the land in a balanced market.
The subsequent cases examine a series of adjustments, first imposing a 15% inclusionary requirement with no offsetting compensation; Case B shows the result of a density increase with no inclusionary requirement. Case C then introduces an offset in the form of a 25% density bonus (of which 15% relates to the affordable units). In Case A and C, it was assumed that affordable units are identical to the market units (and incur identical costs), this is relaxed in Case D where it is assumed that the affordable units are somewhat smaller and more modest and thus constructed at 80% of the cost of the market units.

In all cases, developer profit is held constant at the $2.25 million determined in the base case. As a result, any of the adjustments flow through to directly change the land value (although to a degree residual value and profitability are intertwined – especially if land already owned).

As shown in case A, imposing a requirement to sell 15% (7 units) at a discounted price of $150,000 generates much less revenue and thus a negative residual land value. A rational developer would not proceed with this development and would not be able to purchase the land (or could do so only if he accepted a reduction in profit to only $1.2 Million, 8% of value).

Case B indicates that if the developer successfully negotiated a rezoning to permit a density increase of 25% to 63 units and there is no inclusionary requirement in place, the residual land value increases significantly to $52/sq ft, compared to $31 in the base case).
Thus the developer would be prepared to bid more than $31 to acquire this land, but is taking a risk since the rezoning is not guaranteed, so would not bid the full $52. The difference between what the developer eventually pays for the land and the base case $31 will flow to increased profit margin – with the developer potentially generating a maximum profit of just over $3.2 million (22% of value).

This clearly demonstrates why property developers lobby to increase development potential. While the developer takes a risk, and may not achieve an increase, in most cases there will be some movement in density (especially is the official plan as a policy of intensification and promotes increased density). Thus the approval process generates significant opportunity for financial gain.

Case C takes back some of this gain – essentially creating a public share of the gain. This is imposed in the form of an inclusionary requirement to provide 15% (7 units) at a prescribed affordable price of $150,000. The net result of this requirement is that the developer generates a small net loss with a residual land value of just under $30 per sq ft. In a competitive efficient market where developers are aware of the inclusionary requirement, a rational developer would offer no more than $30/sq ft for the land.

Case D introduces a realistic adjustment in accepting that the affordable units could be slightly smaller and more modest in design (but still compatible and ideally indistinguishable from market units (e.g. a double unit with a similar façade to singles). This also involves a 25% density bonus and 15% inclusion, but construction costs are lower on the seven affordable units, so the residual value of the land increases to $34, in aggregate an increase of $161,000 which depending on how much the developer pays for the land will enhance profitability.

Clearly adjusting the cost of units, ratios of bonus versus inclusion and the target values of the affordable units will all impact feasibility of inclusion. However at a basic level, Exhibit 1 illustrates how these variables interact and suggests that with the right balance it is possible to design an incentive based inclusionary policy, as have been implemented in many other jurisdictions. In the US, it is the option to generate increased revenue and profitability that has precluded legal challenge and most US systems are designed to ensure that the provision cannot be construed as a “taking” (extraction of profit) and thus subject to constitutional challenge.

At the same time, some opposition from developers, especially at the outset, is not surprising. As shown in case B, the potential profitability of a development with increased density is a direct benefit to the developer. With the introduction of an inclusionary requirement there is a reduction in “potential profit” based on rezoning and thus rational developers will seek to preserve this potential. Nonetheless a well designed inclusionary zoning bylaw can still generate a net benefit. The [US] National Association of Home Builders, which is, at best, sceptical about the concept, states: “most inclusionary zoning laws do not completely deprive the developers of a
reasonable economic use (one of the Supreme Court's criteria) and often seek to provide incentives and bonuses as partial compensation” [Tetreault, 2000]. Analysis of the US experience suggests that open and active consultation with the development industry in refining the economic feasibility of inclusionary provisions has been an important element in the successful implementation of these provisions.

Arguments have also been posited that adding an inclusionary requirement increases cost, which are passed on to buyers and therefore undermines the affordability objective. This argument lacks merit – prices are market (demand) based, not cost based. The market reaction to an inclusionary requirement will be felt in the land market, in the form of lower (or less excessive) bids on property. Currently, anticipated increases in density are capitalized by the market into the land value. An existing land owner does not do anything to enhance the land value, it is the anticipation of the public decision approval authority that causes these expectations, so muting speculative capitalized valuations does not take away any “earned” value; the increased value is entirely a windfall gain for existing land owner. However, the developer that prepares plans and an argument in favour of increased density does expend time and funds and thus earns the right to share some of the gain.

4. Designing a Fair Inclusionary Requirement

Among the elements of an inclusionary policy, reviewed in section 2, the two that are most critical are (1) the definitions and benchmarks for affordability together with the percentage of units required to be affordable; and (2) the range and depth of offsets that can be offered to compensate for the inclusionary requirement. Together these two elements determine the economic impact feasibility of an inclusion policy.

This section explores alternate definitions of affordability and the impacts thereof using the base case project from Exhibit 1.

4.1. Definition of affordability

The 2005 Provincial Policy Statement (PPS2005) under the Planning Act provides an existing point of reference:

Affordable: means

a) In the case of ownership housing, the least expensive of:

1. Housing for which the purchase price results in annual accommodation costs which do not exceed 30 percent of gross annual household income for low and moderate income households; or
2. Housing for which the purchase price is at least 10 percent below the average purchase price of a resale unit in the regional market area;

b) In the case of rental housing, the least expensive of:

1. A unit for which the rent does not exceed 30 percent of gross annual household income for low and moderate income households; or

2. A unit for which the rent is at or below the average market rent of a unit in the regional market area.

**Low and moderate income households** means:

a) In the case of ownership housing, households with incomes in the lowest 60 percent of the income distribution for the regional market area; or

b) In the case of rental housing, households with incomes in the lowest 60 percent of the income distribution for renter households for the regional market area.

Note that the definition of low and moderate use two different income distributions – with ownership housing based on the overall income distribution and the definition in the case of renters based on only the renter population, which generally have lower incomes. This varies from the practice in the US and in the Ottawa Official Plan policy where a single overall income distribution is used but a lower percentile target is often set for renter properties.

In support of the PPS, the Ministry publishes an annual set of table with income percentiles, related derivation of affordable rent and affordable home prices. Using a cross section of six Ontario municipalities, Exhibit 2 examines the resulting prices and rent levels. In addition to the PPS thresholds, it also includes for comparison the upper income limit for eligibility for social housing in the same cities.

<table>
<thead>
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</tr>
</thead>
<tbody>
<tr>
<td>City Toronto</td>
<td>68,500</td>
<td>231,000</td>
<td>313,200</td>
<td>47,700</td>
<td>1,190</td>
<td>889</td>
<td>1,252</td>
<td>36,000</td>
<td>50,500</td>
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<tr>
<td>Region of Peel</td>
<td>90,500</td>
<td>305,500</td>
<td>279,900</td>
<td>56,800</td>
<td>1,420</td>
<td>901</td>
<td>1,145</td>
<td>36,000</td>
<td>50,500</td>
</tr>
<tr>
<td>City of Greater Sudbury</td>
<td>62,900</td>
<td>212,900</td>
<td>120,600</td>
<td>32,500</td>
<td>810</td>
<td>544</td>
<td>754</td>
<td>27,500</td>
<td>42,000</td>
</tr>
<tr>
<td>City of Hamilton</td>
<td>66,300</td>
<td>224,000</td>
<td>207,000</td>
<td>39,500</td>
<td>900</td>
<td>611</td>
<td>879</td>
<td>27,500</td>
<td>42,000</td>
</tr>
<tr>
<td>City of Ottawa</td>
<td>83,900</td>
<td>283,000</td>
<td>223,300</td>
<td>50,100</td>
<td>1,250</td>
<td>763</td>
<td>1,115</td>
<td>32,000</td>
<td>49,000</td>
</tr>
<tr>
<td>Region of Waterloo</td>
<td>75,000</td>
<td>253,000</td>
<td>198,800</td>
<td>45,000</td>
<td>1,120</td>
<td>677</td>
<td>953</td>
<td>27,500</td>
<td>42,000</td>
</tr>
</tbody>
</table>

Source: MMAH Market Housing Branch PPS Information Bulletin Oct 2006. Social Housing Income Limits from CMHC.

CMHC HILs published only for Toronto OMA, Ottawa and then OMAs in rest of province.

Exhibit 2 reveals that in this cross section the average house price and the average market rent are the binding constraints rather than incomes percentiles. In all cases, except Toronto, 10% below average sales price is lower than the affordable ownership price based on the 60th percentile income price. The exception is owner housing in the
City of Toronto, where the high proportion of lower income renter households influences the overall income distribution to generate a relatively lower 60th percentile affordable ownership value while house prices are influenced by proximity to the CBD and are high, in relative terms.

The fact that the average sales price in most cities is significantly below the affordable ownership price based on the 60th percentile means that a price 10% below average becomes the primary benchmark (as it is the lesser of) and suggests that, in most cases, the 60th percentile income is not meaningful.

Again, with the only exception being three bedroom units in Toronto, the “affordable rents” generated from the 60th percentile renter income are also well in excess of average market rent levels, which are the criteria adopted by CMHC as a benchmark for affordability in the federal-provincial Housing Affordability Framework and also the lower criteria in the PPS. 5

While affordability is a relative term, it would generally be acknowledged that the incomes displayed in exhibit 2 would typically not be identified as low and modest incomes nor would most observers define the resulting house prices and rents as affordable, suggesting that a lower threshold may be more appropriate. The incomes represented by the 60th percentile are far in excess of the upper boundary of incomes eligible for social housing.

Ideally planning based inclusionary policies should seek to fill the gap between social housing levels and market prices and rents (i.e. assist households at the margin of market affordability) – essentially the approach adopted in Montreal.

Exhibit 3 compares the 60th percentile criteria to recent sales prices for newly build homes. Custom tabulations were obtained from CMHC to identify sales prices of newly completed singles and semis as well as condominium row and apartment structures. Looking at the median price of condominium units, as well as the upper boundary of the first quintile (20th percentile) singles/semi detached house price, it is evident that the development industry is already producing homes in many markets that are priced below the affordable threshold at 60th percentile income, so this does not represent an onerous challenge.

Further evidence is available from the City of Ottawa, which produces an annual statistical summary of development outcomes and specifically enumerates price levels against the City’s affordable housing official plan guideline – based on 40th income percentile (of all households) for owner housing and the 30th percentile for rental.

5 The median market rent is also the basis for CMHC’s derivation of housing Income Limits, so any affordability benchmark premised on average market rent will approximates the Housing Income Limits (HILs). Slight variations between median and averages will however result in some variation.
housing. In Ottawa in 2005 and 2006, respectively, 50.4% and 56.9% of new ownership units (including row and condo) were below the price criteria generated from the 60th income percentile. Moreover, 13.4% in 2005 and 19.9% in 2006 were below the 40th income percentile derived price.

The rental sector is a greater challenge as the economics of rental development are not favourable and rental competes for land with condo projects – so there is a low level of rental production in all cities across Canada. In Ottawa it was not possible to assess success of the City policy (30th percentile income criteria) as insufficient private rental properties were constructed (CMHC suppressed data for confidentiality).

The issue of low rental supply in all markets is a critical challenge (nationally fewer than 10% of total housing starts since 2000 were intended for the rental market). So any inclusionary policy that is more onerous for rental than ownership products (i.e. uses lower percentile or rent based threshold) may have a counter productive effect and discourage an already low level of new rental supply. So greater caution is required in designing inclusionary criteria for developments that might be directed to the rental sector (ideally these should include incentives to overcome less attractive economic feasibility compared to ownership units).

So, for ownership units at least, a policy based on a lower income benchmark than that currently included in the 2005 PPS (60th percentile) seems realistic and appropriate. If the intent is to increase (and balance) overall supply in favour of lower price/rent units the policy should seek to push the envelope rather than simply embrace what the development industry is already producing.

The use of dual price and income criteria (i.e. lesser of), as currently included in the PPS does provide an effective way to overcome the current high income criteria and is a practice that should be maintained to provide flexibility in different markets. Ottawa for example has very high median incomes but lower costs than Toronto; while in Toronto incomes are lower but costs and prices higher.
It is also important to note that while policies directed to addressing affordability must take incomes into consideration; house prices are not cost-driven they are set by the market demand, and reflect willingness and capacity to pay. So, criteria based on rent statistics or house prices are often more meaningful than income criteria.

There is also a challenge in Canada in generating good transparent data on annual income levels as Statistics Canada does not produce a data series with current income for households. Published data based on tax filer incomes is typically 18 months to 2 years old but does not distinguish renter only households. Meanwhile, census data can be as much as eight years out of date (in 2007 still using 2001 census which collected 2000 incomes).

In generating the PPS tabulations the Ministry applies the overall CPI to 2001 census data, so incomes and affordability is based solely on estimates and does not necessarily incorporate actual trends in income. Generating updated income distribution by tenure (separate renter series) is fraught with data constraints and therefore relies on rough estimates which previous work has shown to be inaccurate (Lampert and Pomeroy 1996). In particular, significant variance was found in the projected versus actual trends in renter household incomes.

So, if an income-based criteria is to be used, a single series based on all households (i.e. not separate series for owners and renters) is less vulnerable to distortions and can be more easily updated with income data such as a tax filer family income change index.

4.2. Modelling the Options

Continuing with the previous base case (from Exhibit 1), the effect of alternate affordability targets is now examined, using the 30th, 40th, 50th percentile income and two inclusion ratios 15% and 25%. Two potential offsets are also explored: a density bonus of 25% and waiving fees and development charges on the incremental units.

This analysis first explores the economic feasibility of inclusion on ownership units for sale. A subsequent section then investigates the situation with a modest rental property

**Affordable ownership dwellings**

The base case assumes a 50 unit multi-unit development (before density bonusing). While hypothetical, it reflects norms in mid-higher cost markets like Ottawa and Toronto: sales values at $300 per sq ft; land costs of $30 per sq ft and construction costs at $180 per sq ft reflecting upper mid price range product. Subsequently a slightly more modest cost example is added.

Soft costs are estimated at 15% of these hard costs (excluding GST). These soft costs include public fees and levies which are extracted as a separate value to determine the
extent to which waiving fees and charges is a sufficient offset to compensate for inclusion. Land is at $30 per sq ft (30,000 per unit) and a contingency of 10% is included. A 15% developer/builder margin is assumed. Since the developer profit margin included in costs, total cost equals market value (in the aggregate $15 million for this 50 unit project).

In the scenarios the land value is held constant (presumes land was purchased based on current allowable density) as is the develop/builder profit so the impact of first imposing an inclusionary requirement and subsequently allowing increased density can be explicitly identified as a separate impact (and which would have the effect of lowering or improving developer profit).

With the base price of the unit of $300,000 the impact of requiring inclusion based on the four income deciles from 30% to 60% is examined using the income distribution for the Region of Waterloo (a mid range region).

Corresponding derived prices are taken from the same PPS 2005 tables generated by the Ministry (Oct 2006). As in the earlier exhibit, it is assumed initially that costs for the affordable units are identical to those for the market units; this is later relaxed with the affordable units assumed at 80% of the cost, reflecting smaller units and more modest design.

A detailed exhibit in the appendix presents all the related data, which is summarized in Exhibit 4.

<table>
<thead>
<tr>
<th>Affordability thresholds used</th>
<th>income</th>
<th>price</th>
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<tbody>
<tr>
<td>30th</td>
<td>40,800</td>
<td>137,500</td>
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<tr>
<td>40th</td>
<td>51,000</td>
<td>172,000</td>
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<tr>
<td>50th</td>
<td>62,800</td>
<td>212,000</td>
</tr>
<tr>
<td>60th</td>
<td>75,000</td>
<td>253,000</td>
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</table>

6 In generating price values the Ministry assumes 25 year amortization at 6% and a gross debt service ratio of 30%. However the GDS includes an allowance for the amortized cost of mortgage insurance, property taxes as well as principal and interest. As a result the derived prices actually reflect roughly 26% of income as the base payment for principal and interest.
Exhibit 4: Summary of Alternate Affordability Scenarios at Varying Percentile Price Targets - Ownership Dwellings

<table>
<thead>
<tr>
<th>Assume:</th>
<th>Lot size (200x240) sq ft</th>
<th>Ave Unit size (net)</th>
<th>Market price =</th>
<th>30th</th>
<th>40th</th>
<th>50th</th>
<th>60th</th>
<th>75th</th>
<th>90th</th>
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<tr>
<td></td>
<td>48,000</td>
<td>1,000</td>
<td>$300,000</td>
<td>40,800</td>
<td>51,000</td>
<td>62,800</td>
<td>75,000</td>
<td>85,750</td>
<td>125,000</td>
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<table>
<thead>
<tr>
<th>Price based on percentile incomes</th>
<th>Case A</th>
<th>Case B</th>
<th>Case C</th>
<th>Case D</th>
<th>Case E</th>
<th>Case F</th>
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<td><strong>Income</strong></td>
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<td>Base Case</td>
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<tr>
<td>Inclusion only</td>
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<tr>
<td>25% Density Bonus</td>
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<td><strong>Cost</strong></td>
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<tr>
<td>Total costs</td>
<td></td>
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<tr>
<td>Total public fees and levies **</td>
<td></td>
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<td>Per unit public fees and levies ***</td>
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<tr>
<td><strong>Price on 60th Percentile Income</strong></td>
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<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
<tr>
<td>Market value (anticipated)</td>
<td>15,000,000</td>
<td>14,671,000</td>
<td>14,436,000</td>
<td>18,900,000</td>
<td>18,524,000</td>
<td>18,289,000</td>
<td>18,289,000</td>
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<tr>
<td>Impact on total costs</td>
<td>(328,000)</td>
<td>(354,000)</td>
<td>975,000</td>
<td>599,000</td>
<td>384,000</td>
<td>939,000</td>
<td>948,000</td>
</tr>
<tr>
<td>Impact per affordable unit</td>
<td>(47,000)</td>
<td>(47,000)</td>
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<td>74,875</td>
<td>28,000</td>
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<td>Per unit impact of inclusion (all units)</td>
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<td>(11,280)</td>
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<td>5,778</td>
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<td>Impact as % market value</td>
<td>-2.2%</td>
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<td>6.5%</td>
<td>4.1%</td>
<td>2.0%</td>
<td>5.2%</td>
<td>5.2%</td>
</tr>
</tbody>
</table>

| Price on 50th Percentile Income   | 212,000 |       |       |       |       |       |       |
| Market value (anticipated)       | 15,000,000 | 14,394,000 | 13,944,000 | 18,900,000 | 18,196,000 | 17,756,000 | 17,756,000 |
| Impact on total costs            | (616,000) | (1,056,000) | 975,000 | 271,000 | (169,000) | 831,000 | 416,000 |
| Impact per affordable unit       | (88,000) | (86,000) | n/a | 31,375 | (13,000) | 78,375 | 32,000 |
| Per unit impact of inclusion (all units) | (12,330) | (21,120) | 19,500 | 5,420 | (2,633) | 10,016 | 6,003 |
| Impact as % market value         | -4.3%  | -7.8%  | 6.5%  | 1.3%  | -1.3% | 5.5%  | 2.3%  |

| Price on 40th Percentile Income   | 172,000 |       |       |       |       |       |       |
| Market value (anticipated)       | 15,000,000 | 14,104,000 | 13,464,000 | 18,800,000 | 17,136,000 | 16,787,000 | 16,787,000 |
| Impact on total costs            | (868,000) | (1,328,000) | 975,000 | 217,000 | (195,000) | 881,000 | 416,000 |
| Impact per affordable unit       | (128,000) | (126,000) | n/a | 6,125 | (53,000) | 38,375 | (8,000) |
| Per unit impact of inclusion (all units) | (17,920) | (30,720) | 19,500 | (980) | (10,357) | 4,937 | (1,651) |
| Impact as % market value         | -8.2%  | -11.4% | 6.5%  | -2.3% | -4.8% | 0.2%  | -3.3% |

| Price on 30th Percentile Income   | 137,500 |       |       |       |       |       |       |
| Market value (anticipated)       | 15,000,000 | 13,862,500 | 13,050,000 | 18,800,000 | 16,876,500 | 16,000,000 | 16,000,000 |
| Impact on total costs            | (1,137,500) | (1,950,000) | 975,000 | 325,000 | (1,137,500) | 350,000 | 252,500 |
| Impact per affordable unit       | (162,500) | (162,500) | n/a | (40,620) | (87,500) | 4,375 | (42,500) |
| Per unit impact of inclusion (all units) | (22,750) | (36,000) | 19,500 | (6,500) | (18,005) | 556 | (8,770) |
| Impact as % market value         | -8.2%  | -14.9% | 6.5%  | -2.3% | -4.8% | 0.2%  | -3.3% |

**Notes**

- It is assumed all units are identical and incur same cost (except option D where affordable units at 80% cost reflecting smaller size)
- * * * Developer profit and land value held constant, so any profit identified in impact line (a negative value will reduce profit; a positive value enhance it).
- **Public fees and levies incl Park (5%/land), Building and Development permits ($12/$1,000 cost) and Dev Grp ($6,500 per unit)

As would be expected the lower the affordable price percentile the greater the cost to the developer to include these units (i.e. the differential between the affordable value and what it costs the developer to produce the unit). The aggregate impact also increases as the percent of affordable units increase.

The scenarios begin with the base case and inclusion of first 15% and then 25% units at the specified affordable prices, but with no offset to compensate the developer. The total impact at the project level (50 units in base case) is identified and then specified as a cost per each affordable unit, representing the per-unit cost to the developer to produce the affordable units. It is also presented as an average cost spread across all units in the project and as a percentage of market value of the total property.

As revealed in Exhibit 4, with a 15% inclusion (Case A) the market value declines for each level of income decile of affordability. At the 60th percentile based price ($253,000)

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the impact per affordable unit is $47,000; at the 30\textsuperscript{th} percentile based price ($137,500) the impact is $162,500 per unit. Both reduce the developer’s profit representing declines of 2.2% and 8.2% of market value respectively.

It is notable that at the 15% inclusion rate for affordable units priced at the 50\textsuperscript{th} percentile and lower, the impacts of inclusion far exceed the estimated level of public fees and charges included in costs (roughly $10,160 per unit across all units). However at the 60\textsuperscript{th} percentile threshold, waiving fees and charges on all units in the development would more than offset the cost of inclusion ($6,580). The amount of public fees and charges is not however sufficient to offset impacts when the inclusion rate is raised to 25% (Case B). A larger offset is required.

Case C explores the potential of a 25% density bonus and in order to identify the value of this increased density does not require any inclusion. This results in an increase in aggregate sales value to $18.9 million, and increase in profit per unit of $19,500 (6.5%). This is the gain from increased density and is available to offset and inclusion.

Case D and E assume the affordable units included at 15% and 25% respectively remain identical to market units.

As detailed in Exhibit 4 and illustrated below in the Exhibit 5 chart, at the two higher percentile price thresholds 50% and 60% income) some of the profit from higher density remain with the developer, so there is a positive incentive to include buildings with the affordable units included. At the 40th percentile based price and 15% inclusion, the profit margin is fully erased (Case D and E). So any threshold approximating 40\textsuperscript{th} would extract profit from the developer. At the higher 25% inclusion rate, this impact is negative at the 50\textsuperscript{th} threshold.

However, relaxing the assumption of identical design, Case F and G accordingly assume a cost at 80% of the market units. This restores some profitability at the 15% inclusion rate for the 40\textsuperscript{th} percentile based price and at 25% inclusion becomes marginally negative (-0.1% of market value) at the 40\textsuperscript{th} percentile based price.

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7 This level of fees and charges reflects an apartment size – levies fees and charges are significantly higher on single detached dwellings, especially in greenfield areas where the costs of growth are higher. See Lampert, 1999 Levies Fees and Charges
So overall, assuming a bonus of 25% it appears that if the developer is given some flexibility to revise the design and quality of the affordable units for this median to upper quality property it is possible to implement inclusionary policies in some combination of 15% at the 30th percentile based price or 25% at the 40th percentile price.

Exhibit 6 presents the similar summary impacts for a lower cost more modest development reflecting a non prime location or lower cost city. Still 50 units, in this case the market value is assumed to be $200,000 and costs are lower (land at $21 per sq ft; construction at $120 per sq ft; and soft costs accordingly reduced as a percentage of hard costs).

In this second example a different lower set of incomes and derived prices are used, based on the lower Toronto incomes, but reflective of a number of smaller cities.

In Exhibit 6 because the base market price is lower and already below the 60th percentile price, only the impacts for the 30th to 50th percentile based prices are included. The gap between this market value and the lower percentile based price levels is less and thus easier to achieve. Thus it is feasible to develop 25% affordable units at the 40th percentile based price, even with identical units. However, because this is already modest construction, there may be less room to reduce size and quality of affordable units, even though this option is included in the Exhibit and suggests that with some reductions it

<table>
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</tr>
<tr>
<td>60th</td>
<td>68,500</td>
<td>231,000</td>
</tr>
</tbody>
</table>
might be possible to approach the 30th percentile price before having a negative impact on profitability (a disincentive).

![Exhibit 6: Impact of alternate inclusion and bonus options on market values at range of affordability percentiles with $200,000 modest priced unit and lower income distributions](image)

In both cases (higher quality and more modest), since the developer is concerned about the overall marketability of the property, there is a natural constraint on the developer to maintain a minimal quality so it is likely that the affordable units will be undertaken in a way that does not detract from the marketability of the market units. With the exception perhaps of minimum unit sizes it is not desirable or effective to impose prescriptive conditions on the developer. That said, it is less expensive to build small units (bachelor one-bed units compared to 3-bed), so there is a risk that, without some guidelines, the affordable units produced will not be family sized units. Again, this can be addressed using some criteria that require consistency with the overall project unit types – so if it is a 2-3 bed row development, the majority of the affordable units should be family oriented row units.

**Affordable Rental Dwellings**

As suggested earlier the application of a more stringent affordability criteria in the case of rental properties (e.g. the PPS use of the renter income distribution or average market rents) must be undertaken with some caution.

Numerous studies on the economic feasibility of new rental construction have clearly demonstrated that the economics of new rental development are tenuous (see for e.g. Lampert and Pomeroy, 1997; Clayton Research, 1999; Lampert, 1999; Lampert and Pomeroy, 2001). Experience under the recent federal-provincial Affordable Housing Initiative, which uses capital grants to buy down rents to the average market benchmark
has also demonstrated the level of subsidy required to achieve the threshold of average market rent. In most Ontario cities grants and waived fees and charges close to $50,000 are necessary and, where municipalities have sought deeper levels of affordability, significantly higher grant amounts have been necessary. This reveals the fiscal challenge and resistance when developers are required to provide affordable rental units at the average market level without compensation.

Assessing the feasibility for inclusion in the rental context requires a slightly different approach because unlike sales where the price differential is the main determinant of impact, in the rental case the lower affordable rent levels impact the capacity of the project to secure financing. At lower rents the net income and supportable mortgage declines and requires larger equity investment, impacting the developer’s return on equity. Accordingly, the basis for this assessment is the impact on the amount of developer equity required per unit together with the developers return on equity.

A similar 50 unit development is retained. Costs are assumed to be similar to the second lower cost case study but are further adjusted to remove the developer profit margin. In rental development profit is taken in the form of future return on equity rather than immediate sales revenue. Thus the average per unit cost is $170,000. In the bonus cases, costs are increased proportionately, except that the base land cost is held constant (as in the ownership cases). A market rent level of $1500 per month is assumed, reflecting a 2-bed plus unit in a good location.

Four rent scenarios are used:

- Rent based on the one-bedroom average market rent (Toronto 2006)
- Rents derived at 30% of income based on the 30th percentile income (all households)
- Rents derived at 30% of income based on the 40th percentile income (all households), which also approximates the two bedroom average market rent in Toronto in 2006.
- Rents derived at 30% of income based on the 60th percentile renter income (as per PPS 2005)

The income percentiles are also based on the MMAH published percentile incomes (PPS Bulletin October 2006). For illustrative purposes, both the 60th percentile renter income and 40 percentile overall income are used. As suggested earlier, it is simpler to use a

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8 This reflects the second, lower cost condo development which was priced at $200,000 including $20,000 for land, $120 per sq ft for construction, $18,000 soft costs, contingency of $12,000 and $30,000 developer profit margin. Here the developer profit is removed and replaced with future cash flow as a return on equity, generating a base cost of $170,000 (profit is not eliminated, it is just generated in a different way). This reflects wood frame construction and may be more typical of a suburban location, not downtown Toronto)
single income distribution (based on all households) and these two thresholds are roughly comparable.

In each case an assumed operating cost of $400 per month is used and subtracted from the gross rent to generate a net operating income (NOI). The NOI is then used to determine the maximum level of mortgage financing that can be leveraged at a rate of 6% over 25 years assuming a gross debt service ratio of 1.1. The difference between the total cost and the maximum financing is the amount of cash equity the developer must invest. As rents decline to more affordable levels, the NOI and total financing will be lower and equity requirements increase commensurately.

In addition to being a minimum lending criteria, a GDS of 1.1 leaves a portion of the net income as cash flow and is compared to the level of equity investment to determine the cash-on-cash return on equity (RoE). A minimum RoE of 8-12% is required before a developer will proceed with a rental project.

The same mix of inclusionary and bonus options as used in the ownership case are retained, again beginning with inclusion and no offset (Case A and B), bonusing with no inclusion, then moving through cases with both inclusion and offsets but assuming identical cost units (Cases E&F) and finally assuming more modest design and size.

The summary results are presented in Exhibit 7. In the base case, the specified parameters generate a barely acceptable return of 8.7% and suggest a developer might proceed with this project if he anticipates upward trends in rents. As can be seen in case C where no inclusion is required, the additional revenues from bonused units generate a large enough net income to leverage 97% of the cost – this would not in practice be possible, the lender will require some level of equity investment to achieve a minimum 1.1 GDS, but cash flows will be very healthy, and create room for inclusion.

In the base case the developer must invest $687,500 ($13,700 per unit) in cash equity and this becomes the benchmark against which the other options are assessed.

In case A and B which have inclusion of 15% and 25% with no offset, the amount of developer equity increases significantly and in the lowest rent scenarios more than doubles with 15% inclusion and triples with 25%). Even in higher rent thresholds such as a rent based on the 60th percentile renter income a 15% inclusion still requires a much larger equity investment and results in very unfavourable return on equity.
When a 25% bonus is provided and before any inclusion, there is a very positive effect, with low equity required (with aforementioned caveat) and a strong cash flow. Once inclusion is reintroduced in case D (15% inclusion) the equity required does increase but is lower than in the base case so that the developer’s return on equity is more favourable at 10.9% in the highest affordable rent scenario. At a 25% inclusion rate, the benefit is erased and the project falls to an unfavourable level of return.

Finally assuming the developer is able to introduce some cost efficiencies in the affordable units (smaller size and more modest quality) equity required and rates of return are more favourable across all scenarios except the lowest rent threshold based on the average one-bedroom rent.
These outcomes are presented graphically in Exhibit 8. This highlights the point at which inclusion may be economically feasible:

- 15% inclusion with rents based on the 40th income percentile, a 25% density bonus and no flexibility in unit size or quality; or
- 25% inclusion at the same percentile threshold and latitude to adjust cost and modesty for affordable units.

This assessment was based on a realistic cost estimates (total $170,000 per unit; but $157,000 for the affordable units in case F and G) and a fairly strong rent level. At lower rents of $1,200-$1,400 the initial viability is highly questionable.

In lower cost centres that can build wood frame and achieve costs of under $150,000, it is unlikely that rents will exceed $1,000 so again base feasibility is questionable. 9

In high cost markets where premium rents are achievable the market units help to carry the affordable units, but it is difficult in such markets for rental development to compete for land against condominium options.

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9 For example assuming a base cost of $130,000 per unit, and a market rent of $1000, the low level of leverage results in developer equity required of $45,000 and a first year rate of return of only 1.5%. 

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4.3. Summary and Observations on Economic Feasibility

These illustrative examples, based on the relatively high affordability benchmarks currently embraced in PPS 2005 indicate that even at these thresholds feasibility of inclusion at much more than a 15% rate becomes questionable.

Where low income criteria, such as the one-bedroom average market rent were used, the differential between the value of market units and the cost of building affordable units is generally too large to be feasible. It is clearly not realistic to establish deep targeting criteria in inclusionary policies, without specific subsidy or equivalent offset. The approach adopted in Montreal which seeks to use incentive based negotiated inclusionary targets as a way to complement social housing investment and fill the next rung of the affordability continuum has strong merit. Another option is the approach in Montgomery County where the affordable units are sold at the affordable price to the local housing authority which in turn can add rent supplements and offer these units as a scattered site rental portfolio. This has the benefit of a greater degree of mix and avoids issues of concentrated poverty.\(^\text{10}\)

Actual development outcomes suggest that the criteria of affordable new housing priced on the basis of the 60th percentile income is not meaningful. The industry is already achieving this objective in many markets. Thus a lower threshold is appropriate and, if based on income the 40th percentile of the income distribution (all tenures combined), seems to be feasible. If an income based criteria is used, it should be restricted to a single income distribution for all households. Creating a separate renter distribution cannot be supported based on existing and anticipated Statistics Canada data series.

Alternatively, the existing PPS criteria of the lesser of an income percentile (here 40th suggested) or (a) 10% below average resale house prices for ownership housing or (b) the average rent for a two bedroom apartment in the case of rental properties may also be appropriate (the two bed rent is higher than bachelor or one bed but more realistically achievable).

In the illustrative case studies a consistent bonus of 25% was assumed. Across two ownership cases and a rental property, the combination of this 25% bonus and a 15% inclusion, in combination with a 40th percentile based price or rent appeared to be the approximate breakeven point where there remains a modest incentive for the developer.

Alternate bonusing levels are likely to occur. However, the findings here suggest that when inclusion extracts more than two-thirds of the benefit of higher density, the

\(^{10}\) This approach may also generate economies in development costs, compared to a smaller non profit development. The private builder operates at scale and has the benefit of “free land.” Also there have been recent concerns that the capacity of the non-profit sector to undertake new development has eroded so utilizing the expertise of private builders helps to address this capacity constraint.
development becomes unfeasible. If alternative forms of offset are provided, such as waiving municipal fees and charges, the level of inclusion may have to be adjusted downward to reflect the lower compensating benefit of that option.

Providing the developer some latitude to adjust size and quality of affordable units without too much prescription will help the industry to be creative in balancing the achievement of affordability objectives with marketing considerations.

5. Conclusions and Recommendations

Inclusionary policies are not a panacea to address the issue of supply of affordable housing. However, as part of a broader set of options it can be an important part of a comprehensive strategy to respond to persisting need for affordable housing.

This paper provides a survey of existing practice on inclusion in other jurisdictions and explores options for adapting elements of these practices to the Ontario context. In this respect, it is a discussion paper of policy options and possible initiatives. The authors anticipate and encourage all stakeholders, including legal experts, developers, municipal planners and affordable housing advocates to critically review and debate the recommended proposals to strengthen and clarify the existing legislation.

The legal framework will need to be clarified by a team of legal experts. It would be beneficial for the province to draw on legal experts in Planning Law and Real Estate in Ontario to clarify the need for and extent of legislative change that is required to implement a quasi-mandatory, incentive based inclusionary policy system (i.e. mandatory if developer seeks rezoning or subdivision approval on site above a specified minimum threshold), while also addressing the policy issues described below.

In Canada, municipalities are governed by enabling provincial legislation; they are creatures of their respective provinces. Any municipal powers must derive from provincial legislation and the legislation must be precise and clear as to these powers. In the absence of such explicit authority, the municipal bylaws can be challenged and possibly invalidated.

In the case of incorporating affordable housing inclusion as part of the development approval process, it is critical to clarify the need for, and nature of, the provincial legislation framework. In short, whether mandated, based on incentives, or a combination of the two, it is recommended that the province revise and clarify legislation to ensure that municipalities have the full authority to implement inclusionary policies of their choice.

Once the enabling legislation is in place, one of the most important decisions facing municipalities will be to determine whether the powers to zone for affordable housing
should encompass mandatory programs (i.e. apply to all development over a specified site size or unit count), a combination of mandatory and incentive based programs, or be limited exclusively to incentive based programs. The conclusion in this report is that a hybrid approach is preferable – a legislative framework that permits municipalities to impose prescribed affordability outcomes, with appropriate offsets, in any development involving rezoning or sub-division approval.

It is anticipated that in metropolitan regions (over 100,000 population) the majority of new development will take place either on greenfield sites, requiring subdivision approval; or on infill or brownfield sites requiring rezoning. Supported by appropriate enabling legislation (as outlined below) a municipality would have the authority to establish a policy specifying inclusion of affordable housing in these two situations with guidelines on the target level (percentage inclusion) and level of affordability that is expected – but with flexibility and latitude to negotiate on a site specific basis. For example if a larger density bonus was being contemplated it may be reasonable to negotiate a higher percentage of affordable units, or deeper pricing for increased affordability.

Our assessment in this paper is that offsets based programs that are premised on providing 15% affordable ownership housing units in return for a 25% increase in density, while targeting households incomes in the 40th percentile would, on average, result in reasonable returns for developers. Similarly a target of 15% for rental developments can also work, if a minimum 25% density bonus (or equivalent compensation) is provided. However we caution the use of deeper targeting in the case of rental properties (as is currently the case in PPS 2005) as this can act as a deterrent to rental supply where the economic feasibility is already quite tenuous, especially when competing for land against condominium ownership products.

Other forms of offset could also be explored. However in most cases waiving municipal fees and charges may not be sufficient, by itself.

However it is critical to include offsets or incentives as a core aspect of any inclusionary zoning program.

Once the nature of the mandatory/incentive question is determined, the resulting changes to the legislative/regulatory framework could include elements of some or all of the following:

- Clarification in Section 2 of the Planning Act (Provincial Interest) that the “adequate provision of a full range of housing” includes particularly the provision of affordable housing and that this is required to address the provincial interest.

- Changes to section 1.4.3 to the Provincial Policy Statement to clarify that inclusionary zoning powers are available to municipalities to assist in “implementing minimum targets for the provision” of housing that is affordable to low and moderate incomes
and that the powers under Section 37 (bonusing) of the Planning Act are available to achieve this as well.

- Clarification in Section 37 of the Planning Act that “affordable housing’ is explicitly considered a “facility, service or matter” that may be required by a municipality in return for increases in height or density of development and that such provision can be secured by way of an agreement.

- Clarification that the “conditions” referred to in Section 34 (16) of the Planning Act as amended in January 2007, explicitly include the provision of affordable housing.

- Changes to Section 51(23) and (24) regarding Plans of Subdivision to clarity that the provision of affordable housing is one of the criteria that should be considered in the subdivision process and that the provision of affordable housing could be included as a condition of subdivision approval.

- Prepare a model draft bylaw either under the provisions of section 37 and/or Section 34 (16) to be adapted by municipalities for the purpose of achieving affordable housing through zoning.
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## Exhibit A-1: Illustrative case study based on 40th percentile based price and market unit at $300,000

### Assume:

- **Lot size (200x240) sq ft**: 48,000
- **Unit size (net)**: 1,000
- **Affordable price =**: 172,000
- **Market price =**: $300,000

### Price based on percentile incomes

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<th>Base Case</th>
<th>Case A</th>
<th>Case B</th>
<th>Case C</th>
<th>Case D</th>
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### Base Case

- **50 unit project**
- **15% inclusion, no offset**
- **25% density bonus**;
- **No inclusion**
- **15% inclusion**
- **25% density bonus; 15% inclusion (affordable units @80% cost)**

### Market value (anticipated)

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<td>18,900,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
</tr>
<tr>
<td>Case E</td>
<td>300,000</td>
<td>15,000,000</td>
<td>14,104,000</td>
<td>13,464,000</td>
<td>18,900,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
</tr>
<tr>
<td>Case F</td>
<td>300,000</td>
<td>15,000,000</td>
<td>14,104,000</td>
<td>13,464,000</td>
<td>18,900,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
</tr>
<tr>
<td>Case G</td>
<td>300,000</td>
<td>15,000,000</td>
<td>14,104,000</td>
<td>13,464,000</td>
<td>18,900,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
<td>17,876,000</td>
<td>17,236,000</td>
</tr>
</tbody>
</table>

### Notes

* It is assumed all units are identical and incur same cost (except option D where affordable units at 85% cost reflecting smaller size)

** Developer profit and land value held constant, so any impact identified in impact line (a negative value will reduce profit; a positive value enhance it).

*** Public fees and levies incl Park (5% land); Building and Development permit(s)($12/$1,000 const) and Dev Chg ($6,500 per unit)
**Exhibit A-2: Illustrative Case Study with Price Based on 40th Percentile Income and Lower Cost $200,000 Unit Price**

<table>
<thead>
<tr>
<th>Assume:</th>
<th></th>
<th>Price based on percentile incomes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lot size (200x240) sq ft</td>
<td>48,000</td>
<td>30th, 31,400, 115,000</td>
</tr>
<tr>
<td>unit size (net)</td>
<td>1,000</td>
<td>40th, 44,300, 149,500</td>
</tr>
<tr>
<td>Affordable price =</td>
<td>149,500</td>
<td>50th, 55,500, 187,000</td>
</tr>
<tr>
<td>Market price =</td>
<td>$200,000</td>
<td>60th, 68,500, 231,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Case name</th>
<th>Base Case</th>
<th>Case A</th>
<th>Case B</th>
<th>Case C</th>
<th>Case D</th>
<th>Case E</th>
<th>Case F</th>
<th>Case G</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inclusion only</td>
<td>15% inclusion, no offset</td>
<td>25% density bonus</td>
<td>Bonus &amp; Affordable Units 80% cost</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Base case/ unit</td>
<td>200,000</td>
<td>10,000,000</td>
<td>9,646,500</td>
<td>9,394,000</td>
<td>12,600,000</td>
<td>12,196,000</td>
<td>11,943,000</td>
<td>12,196,000</td>
</tr>
<tr>
<td>50 unit project</td>
<td>10,000,000</td>
<td>9,646,500</td>
<td>9,394,000</td>
<td>12,600,000</td>
<td>12,196,000</td>
<td>11,943,000</td>
<td>12,196,000</td>
<td>11,943,000</td>
</tr>
</tbody>
</table>

| Afford Price units | 0 | 7 | 12 | 0 | 8 | 13 | 8 | 13 |
| Market Price units | 50 | 43 | 38 | 63 | 55 | 50 | 55 | 50 |
| Total units | 50 | 50 | 50 | 63 | 63 | 63 | 63 | 63 |

| Market value (anticipated) | 200,000 | 10,000,000 | 9,646,500 | 9,394,000 | 12,600,000 | 12,196,000 | 11,943,000 | 12,196,000 |
| Land Value (constant) | 20,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 |
| Construction costs * | 120,000 | 6,000,000 | 6,000,000 | 6,000,000 | 7,560,000 | 7,560,000 | 7,560,000 | 7,560,000 |
| Contingency (10%) | 12,000 | 600,000 | 600,000 | 600,000 | 756,000 | 756,000 | 756,000 | 756,000 |
| Sft Costs @15%/hard | 18,000 | 900,000 | 900,000 | 900,000 | 1,134,000 | 1,134,000 | 1,134,000 | 1,134,000 |
| Developer profit (15%) ** | 30,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 |

| Developer profit (15%) ** | 30,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 | 1,500,000 |

| Subtotal costs | 200,000 | 10,000,000 | 10,000,000 | 10,000,000 | 11,950,000 | 11,950,000 | 11,950,000 | 11,710,000 |
| Impact on total costs | (353,500) | (606,000) | 850,000 | 246,000 | (6,500) | 486,000 | 383,500 |
| Impact per affordable unit (all units) | (50,500) | (60,500) | n/a | 30,750 | (500) | 60,750 | 29,500 |
| Impact as % market value | -3.7% | -6.5% | 6.5% | 2.5% | -0.1% | 4.0% | 3.2% |
| Total public fees and levies | 447,000 | 447,000 | 550,220 | 550,220 | 550,220 | 547,916 | 546,476 |
| Per unit public fees and levies *** | 8,940 | 8,940 | 8,734 | 8,734 | 8,734 | 8,697 | 8,674 |

| Notes | | |
|-------|---------|
| * It is assumed all units are identical and incur same cost (except option D where affordable units at 85% cost reflecting smaller size) |
| ** Developer profit and land value held constant, so any impact identified in impact line (a negative value will reduce profit; a positive value enhance it) |
| *** Public fees and levies incl Park (5% land); Building and Development permit ($12/$1,000 const) and Dev Ong ($6,500 per unit) |

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### Exhibit A-3: Illustrative Case Study with Rental Property - Rent at 40th Percentile Income and Lower Cost $170,000 Unit Price

<table>
<thead>
<tr>
<th>Afford Rent</th>
<th>1,108</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market rent</td>
<td>1,500</td>
</tr>
<tr>
<td>Operating costs</td>
<td>400</td>
</tr>
<tr>
<td>Afford NOI</td>
<td>707.5</td>
</tr>
<tr>
<td>Market NOI</td>
<td>1,100</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Afford rent based on percentile incomes or average market rent</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Income %ile</strong></td>
</tr>
<tr>
<td>------------------</td>
</tr>
<tr>
<td>30th</td>
</tr>
<tr>
<td>40th</td>
</tr>
<tr>
<td>50th</td>
</tr>
<tr>
<td>60th</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Afford Rent units</th>
<th>0</th>
<th>7</th>
<th>12</th>
<th>0</th>
<th>8</th>
<th>13</th>
<th>8</th>
<th>13</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Rent units</td>
<td>50</td>
<td>43</td>
<td>38</td>
<td>63</td>
<td>55</td>
<td>50</td>
<td>55</td>
<td>50</td>
</tr>
<tr>
<td>Total units</td>
<td>50</td>
<td>50</td>
<td>50</td>
<td>63</td>
<td>63</td>
<td>63</td>
<td>63</td>
<td></td>
</tr>
<tr>
<td>Cost</td>
<td>170,000</td>
<td>8,500,000</td>
<td>8,500,000</td>
<td>8,500,000</td>
<td>10,157,500</td>
<td>10,157,500</td>
<td>10,157,500</td>
<td>9,953,500</td>
</tr>
<tr>
<td>NOI Afford</td>
<td>660,000</td>
<td>627,030</td>
<td>603,480</td>
<td>831,600</td>
<td>793,920</td>
<td>793,920</td>
<td>793,920</td>
<td></td>
</tr>
<tr>
<td>NOI Mkt</td>
<td>7,812,500</td>
<td>7,422,230</td>
<td>7,143,466</td>
<td>9,843,750</td>
<td>9,397,727</td>
<td>9,397,727</td>
<td>9,397,727</td>
<td></td>
</tr>
<tr>
<td>Total NOI</td>
<td>660,000</td>
<td>627,030</td>
<td>603,480</td>
<td>831,600</td>
<td>793,920</td>
<td>793,920</td>
<td>793,920</td>
<td></td>
</tr>
<tr>
<td>Max Financing</td>
<td>687,500</td>
<td>1,077,770</td>
<td>1,356,534</td>
<td>313,750</td>
<td>759,773</td>
<td>1,038,537</td>
<td>555,773</td>
<td>707,037</td>
</tr>
<tr>
<td>Equity required</td>
<td>13,750</td>
<td>21,555</td>
<td>27,131</td>
<td>4,980</td>
<td>12,060</td>
<td>16,485</td>
<td>8,822</td>
<td></td>
</tr>
<tr>
<td>Equity per unit (all)</td>
<td>n/a</td>
<td>153,967</td>
<td>113,045</td>
<td>n/a</td>
<td>94,972</td>
<td>79,887</td>
<td>69,472</td>
<td></td>
</tr>
<tr>
<td>Equity per afford unit</td>
<td>n/a</td>
<td>57,003</td>
<td>54,862</td>
<td>75,600</td>
<td>72,175</td>
<td>70,034</td>
<td>70,034</td>
<td></td>
</tr>
<tr>
<td>Cash return</td>
<td>8.7%</td>
<td>5.3%</td>
<td>4.0%</td>
<td>24.1%</td>
<td>9.5%</td>
<td>6.7%</td>
<td>13.0%</td>
<td></td>
</tr>
<tr>
<td>Return on Equity</td>
<td>-7.9%</td>
<td>-4.7%</td>
<td>15.4%</td>
<td>0.8%</td>
<td>-2.0%</td>
<td>4.3%</td>
<td>1.2%</td>
<td></td>
</tr>
</tbody>
</table>

- **Note**: All calculations are based on a 50 unit project, 15% inclusion, no offset, with a 25% density bonus; 25% inclusion. The data includes rental costs, operating costs, NOI, financing details, and cash returns. The equity required is calculated as the difference between the cost and the maximum financing. The cash return is calculated as the ratio of the NOI to the equity required. The return on equity is calculated as the ratio of the NOI to the cost. The change in equity from the base case is calculated as the difference in equity required from the base case.