Proposed Density Bonus System for Victoria's Downtown Core Area Plan

June 2010

Prepared for:
City of Victoria

By:
Coriolis Consulting Corp.

Table of Contents

Summary

Introduction

The City of Victoria is preparing a new Downtown Core Area Plan to guide land use, urban development, and public realm improvements in the centre of the City.

The planning process has identified locations in which there is potential to increase the density of new office and residential development. The approval of new density is an opportunity to make better use of density bonusing, a mechanism that can generate contributions toward the creation of new amenities and can assist the rehabilitation of heritage buildings.

The City developed a preliminary proposal for a new density bonusing framework for the Core Area and then engaged Coriolis Consulting Corp. to suggest refinements to the proposed system.

Density Bonusing

Zoning regulations define allowable uses, density, building height and other development parameters. In density bonusing, zoning defines a base or outright density that can be achieved without making an amenity contribution, but also defines additional density that can be achieved, at the developer's option, by providing a prescribed amenity contribution. This bonus density is normally developed on the site that provides the amenity contribution. In the case of heritage building rehabilitation, in which bonus density is provided to make the project financially viable, the density bonus is usually transferrable (i.e. sold to another development site) because it cannot be accommodated on the property that is occupied by the heritage building.

The economic rationale for density bonusing is that developers will be interested in obtaining additional density by making an amenity contribution because it gives them the opportunity to earn additional profit by developing a larger project.

Density bonusing can be looked at from the perspectives of all stakeholders in the urban development process:

- Consumers (e.g. people buying homes or renting space) benefit from increased supply.
- The community absorbs some impacts from densification, but also benefits from the creation of new amenities.
- Developers have an incentive to use bonus density, as they can acquire additional development entitlements by providing amenities, thereby increasing the total profit from a project.
- The City makes progress toward its goals of densification and neighbourhood improvement.

- Land sellers receive market value based on their existing zoning, but do not enjoy land value gains from the new density, because this land value gain is the basis for the amenity contribution.

For density bonusing to be effective, the following conditions must be true:

- The additional density should be sound in terms of planning, urban design, and engineering.
- Developers must perceive that the additional density is marketable, physically feasible, and financially attractive.
- The City, the community, and the developer must perceive that there is a reasonable balance between the extra density that is approved and the amenity contribution that is obtained.
- The City must be clear regarding the amenities it wants to achieve and the density it is willing to provide.
- Redevelopment sites must trade in the market based on their existing or base density, so that developers can afford to acquire sites and make an amenity contribution. If developers pay for land based on the increased density, they will have difficulty also making an appropriate amenity contribution.
- The system should be reasonably predictable, consistent, and easy to implement.

Heritage density bonusing works somewhat differently. In this case, the City grants additional density to help make heritage building rehabilitation financially viable. This additional density must be transferrable (i.e. able to be sold to the owner of a different development site), meaning that the City must approve the creation of the new density and approve the receiver sites that are eligible to accommodate the additional density.

Current Approach to Density Bonusing

The City currently uses an approach to density bonusing that was adopted in 1990 as part of the Downtown Victoria Plan. Based on experience with the existing system, there are some shortcomings:

- There is not a clearly defined amount of additional density that can be achieved. Density is approved on a case-by-case basis.
- There is not a clear relationship between the amenity that must be provided and the density that can be achieved. Each project is evaluated individually, so there has been a wide variety of amenity contributions and approved density increases.
- Many possible amenities are eligible for density bonusing, with no defined priorities.

The system could be improved by making it more predictable, more efficient, more consistently applied, and driven by a clear set of priorities for new amenities in the core.

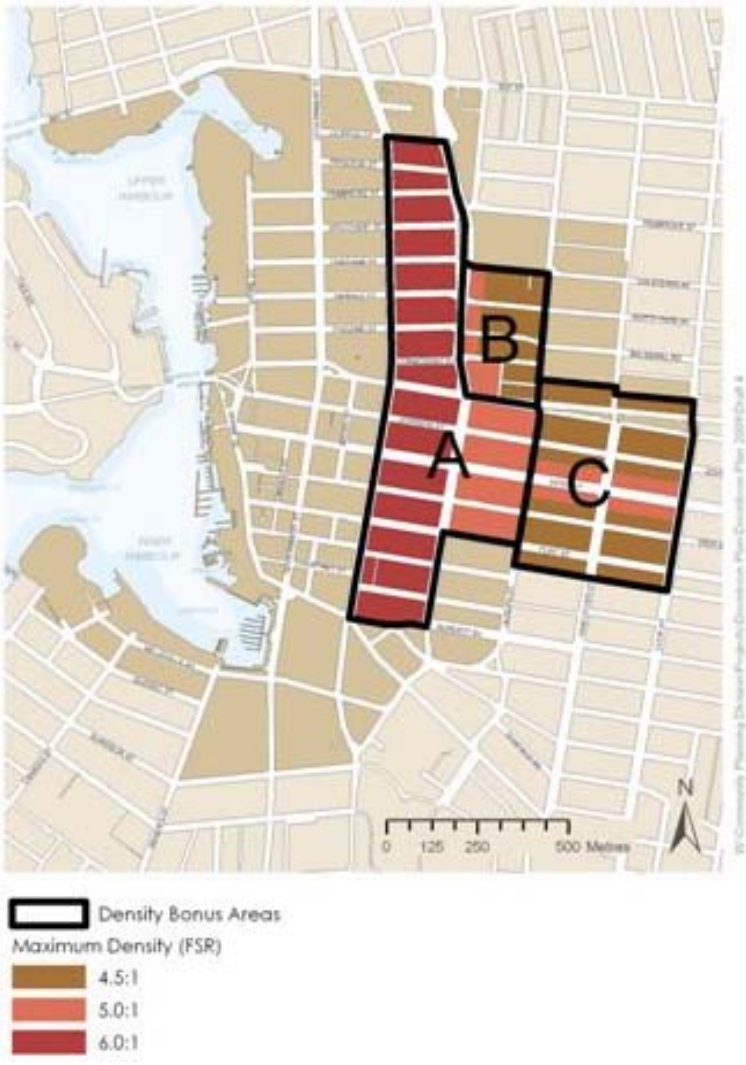
Proposed Amenity Priorities

As part of the core area planning process, the City has proposed these priorities for new amenities: pedestrian network improvements, street beautification and public realm upgrading, public open space improvements, transit corridor improvements, completion of the harbour pathway, and heritage building rehabilitation. These are very good candidates for the use of a density bonus system.

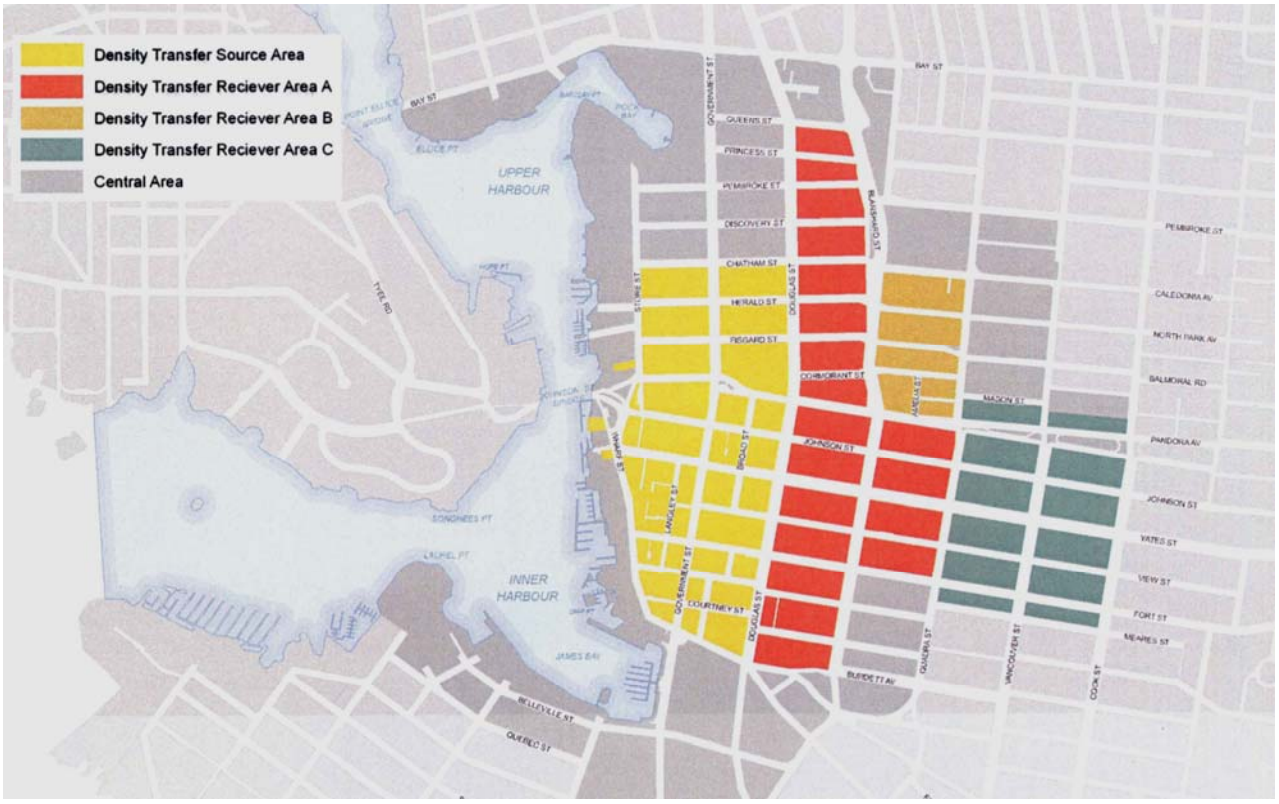
Proposed Density Areas

The City has identified specific areas in which additional density can be obtained. These are shown in the drawing below.

Density Bonus Areas



The City has also identified areas in which it will be possible to absorb transferrable density created to assist heritage building rehabilitation. These are shown in the drawing below.



There is some overlap between the areas in which density bonuses can be earned and the areas eligible for receiving transferrable heritage density.

Because of this overlap, there will be a need to carefully manage the interaction between density bonuses and transferrable heritage density.

We have reviewed the proposed locations for additional density and the proposed size of the achievable density increases and they are generally reasonable.

Potential for Amenity Contributions

We estimate that the City's proposed density bonus framework could generate on the order of $2 million per year in amenity contributions and transferrable density bonuses. The allocation of this revenue between new amenities and heritage rehabilitation will depend on how the City designs the two components of the system.

Recommendations

Waterfront Sites

Waterfront sites are excluded from the City's designated density bonus areas. We agree with this decision because the rezoning and redevelopment of waterfront lands will require site-specific approaches to:

- Achieve on-site amenities such as public access along the harbour and public walkways.
- Deal with design so as to protect water views and waterfront access.
- Produce developments that live up to the outstanding potential of these lands.

Waterfront properties should provide amenity contributions, but these should be determined on a site-by-site basis.

Source Sites in Old Town for Transferrable Density Bonus

Heritage sites seeking transferrable heritage density bonus will have to be negotiated on a site-by-site basis, for these reasons:

- The size of the bonus cannot be determined in advance because the amount depends heavily on individual project economics.
- The bonus must be associated with a commitment (and an acceptable concept plan) for heritage restoration.

Therefore, each case will be individually negotiated.

This is not a problem, as the City already individually negotiates the provisions for property tax abatement, which requires the same kind of financial analysis that will be needed to calculate the appropriate heritage density bonus.

We suggest these refinements:

- The City should revisit its proposed cap of 3 FSR for transferrable density. Some buildings may require more bonus to be viable. If there is a cap for individual projects, it might be better to have a cap on total bonus square footage from any project rather than a cap on FSR.
- The policy should make it clear that a financial analysis must be provided in support of the application for transferrable bonus.
- The policy should make it clear that transferrable density can be used for any uses allowable at the receiver site but that in calculating the initial bonus amount the City will assume the use and value are based on the higher of residential or office land values at the time.
- The policy should require that density bonus is only available if the project has also obtained property tax abatement, to minimize the amount of the required bonus.

To implement this transferrable system, the City must:

- Clearly identify eligible receiver areas.
- Put in place a system to monitor and manage the creation and take-up of transferrable density and watch for any signs of over-supply (which would lead to a deflation in the value of transferable density).

- Create an education plan targeted at heritage property owners, property owners in the receiver areas, and developers.
- Maintain an easily-accessed record of who has transferrable density for sale.
- Establish the legal tools to create the transferrable density at a source site and then shift it to receiver sites.

Receiver Sites Outside of Areas A, B, and C

Receiver sites outside of Areas A, B, and C should be pre-zoned to allow them to "import" extra density.

These receiver sites need a base and maximum density defined in bylaws. Receiver sites should not be rezoned site-by-site because the marketability of the transferrable density would be impaired by rezoning risk.

The City may want to consider expanding this area, because the total amount of land outside A, B, and C is small. One way to expand the receiver areas without dramatic impact on receiver neighbourhoods is to change zoning in a larger area to allow a small increment in FSR (say 10%) without rezoning if the increment is for a heritage transfer.

Areas A, B, and C

We see three alternative zoning approaches to these areas:

1. Site-by-site. The City could rezone these properties individually on application. This means individual negotiations and continued rezoning risk, but the approach is still dramatically better than the current approach, because the base and bonus density (and height and use) will be established in the Plan, as will the amenity priorities and the emphasis on cash-in-lieu. If Council consistently approves rezoning based on OCP policy, this will work. The new approach will not be ad hoc. Because of the heritage transfer system, the City will need the capability (internal or consultants) to do the financial analysis anyway. As well, it is important to note that the total number of projects will not be large (likely 2 or 3 per year based on recent experience), so the total administrative load is not large.
2. Pre-zone. Areas A, B, and C could be prezoned to allow the base and bonus density. The pre-zoning approach will require that the bylaw defines the amenity contributions, which should be initially set at $15 per square foot of office and $30 per square foot of residential, less 25%.[1]

[1] The 25% is intended to make some of the land lift available for assembly, transaction costs, and incentive.

These values are at the low end of the range of current market value to maximize take-up. To implement this system, the City will need a mechanism to periodically update the dollar rates in the bylaw (at least annually) based on market conditions.

This approach eliminates political risk and eases administration. The downside is the loss of the ability to tailor site-specific amenity contributions.

3. Pre-zone, but with a developer option to apply to rezone. To maintain some flexibility for some sites, say those with some unique amenity opportunity, the City could adopt a hybrid approach along these lines:

   - Pre-zone Areas A, B, and C to allow the base densities and bonus densities as proposed above.
   - Identify areas where additional density (FSR 1?) could be available via rezoning under special circumstances on application by the developer (which may come about at the suggestion of the City). In these cases, a site-specific rezoning would determine the density and the amenity contributions.

   Note that in this approach the developer has the certainty of the pre-zoned approach as a fall-back plus the opportunity to obtain more density.

In our view, any of these three approaches would be better than the existing approach and any could be implemented successfully. We lean toward option 3 because of its combination of reduced zoning risk while maintaining some flexibility.

In any approach, the City must address the issue of the mix between heritage and amenity bonus.

In order to ensure a market for heritage density but also to ensure that some amenity contribution is obtained, we suggest that the bonus zone include a cap on the share that can be transferrable heritage density. There should not be a minimum because there may not be heritage density for sale all the time.

We suggest an initial cap of 25% for heritage, but this should be monitored and if necessary adjusted depending on how much heritage density is being created and how much unsold heritage density there is.

Transition Policy

In new density bonus areas not in the current Plan, there is no need for a transition policy (other than a plan to communicate the new system) because the market should not have been pricing in premiums based on upzoning. However, there may be a need for a transition policy in the existing (1990 Plan) density bonus area where it appears that some land sales in recent years have included a premium based on anticipated upzoning. This is a predictable result of the existing density bonus system.

Introducing a new density bonus system in the existing density bonus area means that it is possible that some land owners will have expectations of values being higher than supported by existing zoning and some developers may have "overpaid" for redevelopment sites. To ease the introduction of the new system, the City could consider these transitional options:

- While we suggest pricing density bonus at 75% of market value in new areas, the City could (for an interim period of say 2 years) price bonus density at a lower rate (say 50%) in the existing density bonus area. This provides an extra cushion for developers who recently bought sites under the old regime.
- The City could adopt a two-tiered bonus in the existing amenity area based on the fact that few sites have achieved density over about 5.5 FSR. Bonus density to reach 5.5 could be priced at 50% and density above 5.5 could be priced at 75%, for an interim period.

1.0 Introduction

The City of Victoria is preparing a new Downtown Core Area Plan to guide land use, development, and public realm improvements in Downtown and adjacent core area neighbourhoods.

As part of the Core Area planning process, the City has identified parts of the central city that are appropriate candidates for allowing increased density of development. The City sees additional density as having several planning advantages:

- Higher density will use land more intensively in the core area of the City that is well served with transit, already has a strong pedestrian orientation, and already has civic infrastructure.
- Higher density will make the core area even more transit supportive, presumably facilitating future investments in rapid transit and the bus system.
- Higher residential density will increase the potential for supporting local commercial uses that can make core area neighbourhoods more attractive and liveable.
- Higher office density will help Downtown to maintain its role as the dominant business and government centre in the region.

Increased density of development adds more residents and employees in an area, which has advantages but also can have some negative impacts including increased requirements for new community amenities and increased loads on existing amenities and infrastructure. Therefore, as part of the Core Area planning process, the City wants to ensure that there is a strategy for the funding and creation of community amenities and infrastructure that will meet the needs of new residents and employees and that will help existing residents see benefits from densification in their neighbourhood. Development Cost Charges can be used to fund some basic community infrastructure (such as roads, water, sewer, and park acquisition) but many key components of an attractive and liveable downtown (such as heritage building preservation, streetscape improvements, and community space) cannot be funded with DCCs.

Therefore, as part of the strategy for funding amenities, the City wants to include in the Downtown Core Area Plan a density bonus system that will create incentives for densification while also providing a means to obtain new amenities that will enhance downtown.

The core includes a large and significant heritage district (Old Town) that makes an important contribution to the character and economic strength of Victoria. The history, ambience, and architectural character of Old Town are an important part of Victoria's image and personality. Old Town provides an environment that has been successful as a specialty retail, food/beverage, and entertainment district for residents and tourists. However, the economic viability of heritage building rehabilitation is challenging, partly because of the high cost of seismic upgrading and the relatively low density of many existing historic buildings. The City has an incentive program for heritage rehabilitation that includes small capital grants for facade improvements and multiyear

reductions in property taxes. These two incentives are not sufficient to make some heritage rehabilitation projects viable, though, so the City also wants to use density bonusing as a means of providing additional financial incentives.

Therefore, the City wants to design a density bonus system for the Downtown Core Area that achieves two objectives:

- Provide a mechanism for encouraging densification in new residential and commercial developments while obtaining amenity contributions that enhance the core area and the neighbourhoods expected to absorb new developments.
- Provide a mechanism for incentives for heritage building rehabilitation in Old Town.

The City retained Coriolis Consulting Corp. to help design a density bonus system that would achieve these objectives.

2.0 Basic Elements in the Design of a Density Bonus System

As the starting point in the design of a density bonus system, this section provides an overview of the legislative basis for density bonusing in BC, the urban land economics rationale for density bonusing, and guidelines for a successful system based on actual experience in municipal settings.

2.1 Basics

Zoning regulations typically define the allowable uses, density, height, parking requirements, and other parameters for urban development. Density bonusing adds a new dimension to zoning regulations. Rather than simply define an allowable maximum density, a density bonus zoning regulation defines a base or outright density that can be achieved without providing any amenity contribution and also defines additional density that can be achieved, at the developer's option, by providing a prescribed amenity contribution.

As a simple example, a typical zoning regulation might allow a density of FSR 3.0 on a site designated for high density residential development. In a density bonus system, the zoning would allow a base density of FSR 3.0 but also allow an increase in density, say a gain of FSR 2.0 up to a maximum of FSR 5.0, if a prescribed amenity contribution is provided by the developer.

The urban planning rationale for density bonusing can be summarized as follows:

- A community determines that there are sound planning reasons for encouraging higher densities in a particular neighbourhood than are allowed under existing zoning. The reasons for densification might include increased transit ridership, more potential for a pedestrian-oriented mixed use environment, more intensive use of land and infrastructure, or more support for local commercial uses that make the neighbourhood more attractive.
- Extra density will cause a requirement for additional community amenities to serve new residents or employees. There may also be a need to provide amenities so that existing residents will see benefits from densification, rather than seeing extra development as only causing negative impacts such as more traffic or increased loads on existing amenities.
- The approval of additional density on a development site should (assuming there is a market for the extra space) increase the value of the site.
- Rather than giving this additional land value "for free" (i.e. creating a windfall gain in value for the land owner or the developer) some portion of this additional land value can be converted by the municipality into community benefits.

- Implemented properly, density bonusing can result in higher density development, generate community benefits including amenities, and create incentives for developers by enabling them to build larger projects and earn commensurately larger developer profit.

Note that the implicit assumption in a typical density bonus system is that the approved additional density will take the form of additional development on the site that is generating the amenity. This of course results in additional site coverage, additional height, or both. In the case of providing bonus density for a heritage rehabilitation project, however, it is often not possible to preserve an existing heritage building and also allow the on-site development of additional density, because the heritage building occupies too much of the site to enable the development of new space. In these cases, a heritage-related density bonus requires that the heritage site developer have the ability to transfer the density bonus (i.e. transfer the development entitlements) to another site that is presumably zoned so as to allow the "importation" of extra density. The density could be transferred to another site that the developer owns or sold to a different developer of another site (zoned accordingly) that wants additional density.

2.2 Urban Land Economics Rationale for Density Bonuses

Property values in an urban area are determined by a wide range of factors, but two of the main determinants are the existing use (including the existing improvements) of the site and the redevelopment potential of the land based on zoning or planning policy.

Generally a site is only a candidate for redevelopment if the land value supported by redevelopment potential exceeds the value supported by the existing use. For example, a site occupied with older low density commercial space has one value supported by the rental income the owner would receive from continuing to lease out the commercial space and a different value supported by redevelopment (demolition of the existing improvements and development of a new project).

The value as a redevelopment site is heavily influenced by the development potential (uses, density, height) allowed under zoning or planning policy. In general terms, the more density that is allowed the more valuable the property, assuming that redevelopment is financially attractive and assuming that the extra density is financially viable to develop.

When developers buy development sites, they go through an exercise (called a residual land analysis) to determine how much they can afford to pay for the site based on the expected financial performance of the development project. In this exercise, developers make an assumption about how much development can be accommodated on the property. This assumption would be based on existing zoning or on the perceived likelihood of obtaining a rezoning to allow a change in use and/or a change in density.

If rezoning for more density can be obtained relatively easily and at little cost, the market recognizes this and tends to push up the value of development sites to the level supported by the

anticipated rezoning. If rezoning is perceived as risky, time-consuming, and expensive the market tends to base the value of development sites on existing zoning.

Density bonusing creates a mechanism for additional density, but also creates a mechanism whereby some of the value created by this extra density is captured in the form of community amenities rather than all of it taking the form of higher land values.

Exhibit 1 below contains some simple examples to illustrate this important point.

Exhibit 1: Density Bonus Calculations

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

The numbers used in Exhibit 1 are broadly consistent with market conditions in central Victoria, but should not be assumed to be a precise reflection of current development economics. The point of the exhibit is to demonstrate a principle.

The exhibit shows a simplified financial analysis for the development of a hypothetical multifamily residential project under various zoning scenarios. There are some important assumptions common to all scenarios: the site is assumed to have an area of 20,000 square feet; the site is assumed to be more valuable as a redevelopment site than in its existing use; redevelopment is assumed to be marketable and financially viable; and developers are assumed to be interested in density increases in this location (i.e. the opportunity to make the project larger is appealing).

Scenario 1 assumes the site is zoned to allow an outright density of FSR 3 which can be achieved with no amenity contribution. The market assumes there are no prospects for rezoning to higher density (presumably because the existing zoning is consistent with the Official Community Plan and there have been no approved rezonings in this area to higher density). At FSR 3 the site can be developed with 60,000 square feet of space, which is assumed to work out to 60 units.

The numbers are organized to show that the developer sells the units, deducts all the costs of creating the units including any Development Cost Charges, sets a target for profit (based on a typical industry percentage of revenues), and then calculates the amount the developer can afford

to pay for the site. In this case, the maximum the developer can pay for the land is $2.4 million which works out to about $40,000 per residential unit or about $40 for every square foot of developable area allowed under existing zoning.

Scenario 2 shows what would happen if the site had already been rezoned to allow a higher density (in this case FSR 5) or if the prospect of rezoning to FAR 5 is regarded by the market as highly likely (i.e. not risky) and relatively inexpensive, with no requirement for an amenity contribution. In this case, the additional development potential means the developer is willing to pay more for the land ($4.0 million rather than $2.4 million), although note that the new higher land price is still $40,000 per residential unit or $40 for each square foot of allowable development potential. Note also that the developer earns a larger profit (although it is still budgeted in the same way, as a target percentage of projected revenues). The larger profit is warranted by the additional risk of developing a larger and more expensive project that will take longer to build and sell.

In this second scenario there is no amenity contribution. The community has achieved the goal of densification (the site accommodates 100 units instead of 60), but no new amenities are funded out of the development. Any need for amenities would have to be funded by other sources such as property taxes. In a sense, the higher density has resulted in an opportunity for more developer profit and has created a higher selling price for the person who sold the land to the developer, but has not created any benefit for the community beyond the general benefit of more housing.

Scenario 3 shows how the numbers could work in a density bonus system. In this scenario, the site is assumed to be zoned to allow an FSR of 3 (as in Scenario 1), but in a zoning bylaw that also allows for a density bonus in exchange for a community amenity contribution. In this scenario, it is assumed that the available bonus density is 2 FSR, so maximum project density is FSR 5, the same as in Scenario 2. The developer in this case is assumed to use the maximum available bonus and, in this hypothetical density bonus zone, the developer is assumed to make an amenity contribution equal to the full market value of the density bonus (i.e. the full market value of the land value increase that results from the additional density). The actual amenity contribution could be a physical amenity incorporated in the project, in which case the cost to the developer is the cost of construction, or it could be cash-in-lieu paid to the municipality. The cost to the developer is assumed to be equal in either case.

Scenario 3 illustrates some important points about density bonusing and the impact on urban land markets and housing:

- Note that the developer in Scenario 3 has a total “land” acquisition cost of $4,000,000, or $40,000 per unit. This is made up of $2,400,000 to buy the development site (based on its value as a site with density of FSR 3) plus $1,600,000 in amenity contribution to achieve the additional FSR 2. This is the same total cost to acquire development entitlements as in Scenario 2, but in Scenario 2 all of the cost is paid to the person selling the land zoned with FSR 5.

- Note also that the analysis assumes no change in the sales price of the new housing units. There are not any extra costs that the developer would try to pass on to purchasers (even if the developer could, which is not likely in a competitive market in which prices are set by demand not by cost). In effect, each unit's price includes the cost of the market value of multifamily land, but not any additional cost, so there is no upward pressure on housing prices. In fact, the larger project means more units are developed which could help moderate price growth in the market.
- Importantly, the developer attains the same profit in Scenario 3 as in Scenario 2. There is no erosion of profit from having provided an amenity contribution.

Here is how Scenario 3 looks from the perspectives of all stakeholders:

- Housing buyers benefit from the development of more units.
- The community will absorb some impacts from densification, but the community also benefits from the amenity contribution assuming the amenity is something that enhances the neighbourhood.
- The developer has an incentive to make use of the density bonus, because of the opportunity for a larger project and additional profit (commensurate with the additional risk, but larger nonetheless).
- The municipality makes progress toward its goals for densification and neighbourhood improvement.
- The land owner sells the site based on its value under existing zoning (i.e. the zoning in place before the amendment to allow bonus density). The land owner enjoys whatever growth in value for sites zoned with FSR 3 has occurred since the initial acquisition, but does not get the additional land value from the density bonus.

Scenario 3 assumes that the municipality aims to capture 100% of the land value associated with the bonus density. In practice, it is usually necessary to aim for a lower share (somewhere between 50% and 75% depending on circumstances) for reasons including these:

- If land assembly is required to achieve practical development sites, the developer may need some additional purchasing power to buy all the properties on a timely basis. If the amenity share is less than 100%, there is some money "left in" the project enabling the developer to pay a premium price to assemble sites.
- Leaving some of the extra land value in the project adds the potential for some additional incentive for the developer. True, the developer already has the incentive of a larger developer profit, but dealing with the process of obtaining the amenity bonus adds to the developer's administrative load and increases some costs (e.g. design fees to determine the optimum additional density to seek). Leaving some of the land value gain in the project helps cover these costs.

- Sometimes land owners are not content to sell at market value. If a landowner would have to purchase a replacement property at market value, there may not be any incentive to go through the process of selling, buying, and (if a business) relocating. Developers find that they have to pay a premium price to persuade such owners to sell.

The numbers would be structured quite differently for a transferrable heritage density bonus. The reason for the bonus is to compensate a developer for the extra costs (or reduced profitability) of rehabilitating a heritage building. As well, retaining a heritage building may mean under-using the density already approved on the site (for example, a site may be zoned to allow FSR 3 but the existing heritage building only uses FSR 2. The extra 1 FSR cannot be accommodated on site). The typical approach is to analyze the financial performance of the heritage project and see if a developer can afford to buy the property (at existing market value), complete the rehabilitation project, and earn an appropriate developer profit. If not, the project is not viable. To make it viable, the developer can be granted sufficient transferable density (that can be sold to other developers) to make the project viable. Therefore, such bonuses must be calculated on a site-by-site basis, based on individual project economics.

2.3 Legal Basis for Density Bonusing

The legislative basis for density bonusing in British Columbia is Section 904 of the Local Government Act, which states that a zoning bylaw may establish different density regulations for a zone, with one density generally applicable in the zone and a different (higher) density applicable to sites that meet defined conditions. The allowable conditions include “the conservation or provision of amenities including the number, kind and extent of amenities” or “the provision of affordable and special needs housing”.

Because the legislation states that a density bonus zone should specify the number, kind, and extent of amenity that is to be provided, the legislation could be read to imply that the amenity should be in the form of an actual physical amenity on the development site (such as public open space, day care, social housing, or public art). However, not all development sites are good locations for physical amenities and many development sites are not large enough to physically provide an amenity that is large enough to be useful. For example, rather than have several development sites each providing very small (possibly non-viable) day care spaces, it might be more effective to pool the contributions from various projects to make one day care centre. Similarly if the desired amenity is a larger public facility (say a library) the only viable way to achieve this from density bonusing is to pool contributions from many projects. Therefore, a cash-in-lieu system is obviously useful and the legislation has been interpreted to allow this.

The Provincial government has issued clarifying guidelines regarding the use of density bonusing, particularly when cash-in-lieu is contemplated. These guidelines are summarized below, along with our observations based on experience:

- The amenity should benefit the area in which the new density is located. In our view, this does not literally mean that the amenity must only benefit the local area, because there are cases in which one new amenity (e.g. a community centre) serves a large area and benefits more than just the location absorbing the new density. However, we think the general principle that the amenity must provide some benefit to the area absorbing the density makes sound planning and political sense that lends credence to plans for densification. Neither developers nor existing residents will be too enthused about a system that puts density in one area and exports all of the amenity contributions to another.
- Density bonuses should not be used to fund infrastructure that could readily be funded by other means. For example, density bonuses should not be used to fund the basic community infrastructure than can be funded via Development Cost Charges. We agree with this principle. Municipalities have good tools for funding basic roads and services (e.g. DCCs); they have much more limited ability to fund other important elements of community-building such as libraries, fire halls, public art, social housing, or day care.
- Cash-in-lieu should be used in cases in which there is a strong rationale for creating local amenities that can only practicably be created if contributions from various projects are pooled. This will be true where most development projects are relatively small and/or where the most important community amenities are too large or expensive to be carried by a single project. The Province, wisely, wants to ensure that municipalities do not simply treat amenity contributions as an arbitrary tax on new development.

Density bonusing has been used in BC long enough for there to be some legal interpretations, in the form of judicial decisions and various legal opinions. We don't purport to provide legal advice, but we do have an understanding of the key implications of the jurisprudence for the design of a successful density bonusing system.

There appear to be three tests that a density bonusing system should pass in order to be resistant to legal challenge[2]:

- The amount of additional density to be provided must be clearly defined in the density bonus bylaw at the time of bylaw consideration, particularly at public hearing.
- The amenity that is being provided in exchange for the additional density must be clearly defined at the time of bylaw consideration. This means either defining the nature of the physical amenity to be provided or, if cash-in-lieu, defining the amount of the payment and the proposed general uses of the money. Essentially, an informed citizen should be able to weigh

[2] Given the voluntary nature of using bonus density and the advantages to a developer of tapping the opportunity for more density, it is unlikely that a developer would challenge a density bonus bylaw or the application of the bylaw to the developer's own site. A more likely scenario is that a third party, concerned about the impact of the additional density, might be interested in finding ways to thwart the development of additional density by challenging the zoning bylaw.

the specific pros and cons of the added density and the associated amenity contribution in deciding what stance to take regarding the rezoning.

- There should be a clear link between the creation of additional density and the nature of the amenity (i.e. the amenity should be part of the strategy for creating a higher density area that will need certain amenities to support the increased population or address the impacts on the existing community).

Based on experience, there appear to be two different approaches to the design of a density bonus system that should be legally robust. These two approaches can be summarized as follows:

- Rezone on a site-by-site basis. In this case, the municipality would have policies (ideally adopted in the Official Community Plan) that identify areas in which sites will be considered for rezoning to a density bonus zone. The planning policy would define the base density (presumably consistent with existing zoning), the maximum additional density that can be obtained by density bonus, the kinds of amenities that the municipality aims to achieve via density bonusing, and the suggested mechanism for determining the specific amenity contribution to be obtained from future rezoning proposals. When a developer comes forward with an application for rezoning in the density bonus area, the developer and the municipality would negotiate the terms of the rezoning including the amount of additional density (up to the OCP maximum) the developer wants to obtain, the form and character of the project, and the precise amenity contribution (either an actual amenity, cash-in-lieu, or some combination) to be provided. The entire rezoning proposal (including the density to be granted and the amenity contribution to be made) would be the subject of a public hearing, staff review, and decision by Council. Any interested citizen would have full information about the proposal and would be in an informed position to decide whether to express support, opposition, or suggestions for revision at the public hearing, based on that citizen's perception of the advantages and disadvantages of the proposed development. The City of Victoria currently uses this site-by-site for density bonusing in downtown, although the approach is somewhat ad hoc because there has not been an adopted policy regarding maximum density or priorities for amenities.

- Rezone sites in advance with a clear and formulaic approach to amenity contribution. In this case, the municipality would rezone sites or an entire area into a new density bonus district. The new zoning regulation would define the base density (presumably similar to the pre-existing zoning) and define the maximum additional density that could be achieved. The new regulation would also define the specific amenity contribution to be provided, for example by specifying a menu of specific on-site amenities to be included in projects or by specifying a cash-in-lieu payment (usually expressed in dollars per additional square foot of permitted density).

The two approaches have different advantages and disadvantages.

The site-by-site approach has these characteristics:

- The developer, the community, and the municipality can be sure that the relationship between the amenity contribution and the density provided are thought out in detail for the specific site. The development of a tailored package for each site makes it very easy to design a specific bundle of public benefits and weigh the pros and cons of the larger project, from all perspectives.
- To the extent that the value of the amenity contribution is intended to be commensurate with the value of the extra density, the site-by-site approach allows for an analysis of the specific project at the time of development. This specific analysis allows the developer and the municipality to be accurate about the appropriate amenity contribution that is financially supportable by the proposed rezoning.
- There is still rezoning risk in the project. The site-by-site approach means that each amenity density project is the subject of a specific rezoning application. While such an application would presumably be in the context of clear OCP policy regarding densification and amenity contributions, rezoning nonetheless requires public consultation, public hearing, and dealing with specific concerns such as traffic, view blockage, shadows, privacy impacts, architectural character and other issues that are raised when development proposals involve increased height and density. The site-by-site approach does not guarantee that all rezonings will be approved, creating risk for developers and also creating uncertainty about whether the overall goals for densification and amenities can be achieved.
- The site-by-site design work and negotiations between the developer and the City take time and cost money.

The pre-zoning approach has the “reverse” set of advantages and disadvantages:

- The pre-zoning approach requires defining in advance the amenity contribution and the extra potential density for a wide range of sites. While these can be adapted over time, there still is to some extent a one-size-fits-all approach that may mean a more generic contribution to amenity.
- The value of the amenity contribution will only be approximately commensurate with the value of the density. Land values vary from site-to-site and change over time, but in the pre-zoning approach it is necessary to set a general value for amenity contributions that must apply to all sites in the zoning district. If this number is too low, then this will maximize the number of projects that want to take advantage of density bonusing but may not maximize the total potential value of amenity contributions. If the number is too high, some projects will not use the system. Because of variations in land value from site to site, it is almost inevitable that the number will have to be on the low side to ensure that most eligible sites take advantage of the density opportunity. This approach requires that the amenity contribution is recalibrated periodically to reflect changing land values, if the aim is to ensure that the amenity contribution is consistent with the value of the bonus density.

- The rezoning risk is taken out of the developments. This is a major advantage for developers and possibly for the City (in terms of planning for the full implementation of densification and amenity strategy). To the extent that densification meets with resistance from some stakeholders, the debate is held once for the rezoning bylaw for a whole district. If after weighing the advantages and disadvantages (in planning, technical, and political terms) Council approves the rezoning, then the densification potential for all of the sites in the area is confirmed. In the site-by-site approach, there is a risk that individual density proposals are not approved even if they are consistent with an adopted densification policy, due to localized opposition.
- This approach takes less time and is less expensive to implement, because there is no need for site-by-site analysis or negotiations.

2.4 Factors to Consider in the Development of a Density Bonus System

Based on our experience with designing and implementing density bonus systems, there are some important factors to be considered in the design of the optimum system for a community. These factors can be divided into four categories:

- General conditions that should exist in order for the density bonus system to be effective.
- Municipal objectives that are a good “fit” with density bonusing.
- Elements that will help build acceptance in the development community.
- Ways to ensure that the amenities remain in perpetuity.

2.4.1 General Conditions

4. The extra density must be able to be accommodated on sites in the area selected for densification without unacceptable impacts on urban design, neighbourhood character, traffic, or other factors. In other words, it is necessary to start with a robust community planning and urban design process that identifies appropriate locations for additional density and sets appropriate maximum densities and heights. Bonus density should be a means to provide amenities to support density that is appropriate in planning terms, not an arbitrary basis for adding density just to get amenities.
5. Developers must perceive that the available additional density is marketable, physically feasible, and financially attractive. In weak markets, developers may be reluctant to take on the additional risk associated with a larger project. In strong markets that support development, developers will usually be interested in the chance to increase project size, but there can be circumstances in which extra density does not pencil out. For example, if extra

density requires going one level deeper for underground parking or requires a shift from wood frame to concrete construction, then project economics can be impaired by the extra density.

6. The City, the community, and the developer should perceive that there is a reasonable balance between the extra density that is granted and the amenity contribution that is obtained. There is a qualitative dimension to this assessment, in that the perceived enhancement of the community should offset any reduction in neighbourhood quality due to the added development and population. There can also be a quantitative dimension, if the aim is to make the actual cost or value of the amenity contribution commensurate with the value of the extra density. There are two main reasons for achieving a reasonable balance between amenity cost and density value:

   - If the municipality attempts to obtain too much, developers will not be interested. A developer cannot afford to contribute more than the extra density is worth.
   - If the municipality significantly under-values bonus density, this does not necessarily translate into an additional incentive for developers. The land market is very efficient and fast at capturing the additional value of extra density if it is not captured in the form of amenity contributions. Granting extra density at bargain prices will lead to escalation in land value for development sites. Some of this land value gain may be the premium necessary to facilitate or accelerate land assembly, but in some cases it will simply put inflationary pressure on the value of development sites. The “ideal” circumstance is one which developers pay most of the value of bonus density in the form of amenity contributions and retain some of the value as incentive and/or available premium to facilitate land assembly. In practice, this means setting the value of bonus density somewhere in the range of 50% to 75% of actual market value of the density, depending on local circumstances.

7. The City must be very clear regarding the amenities it wants to achieve via density bonusing. This clarity is needed so that developers know what to include in projects, the community knows what amenities will be achieved to support densification, and the system (and its administration) can be designed as efficiently as possible to achieve the desired amenities. City objectives regarding amenities should be based on an explicit evaluation of:

   - The kinds of amenities that are most needed to enhance a residential or commercial area being densified, meet the needs of new and existing residents in densifying neighbourhoods, or to mitigate the costs and other impacts of growth.
   - The appropriate mix between amenities that serve the whole community versus amenities that mainly enhance the local neighbourhood undergoing densification.
   - The extent to which amenities will be physically accommodated within individual development projects versus created by pooling cash-in-lieu contributions from many projects in order to produce larger amenities in good locations.

8. The combination of allowable base density and available bonus density must result in an acceptable number of sites being financially viable redevelopment candidates. In an already-urbanized area (such as Downtown Victoria) the existing older commercial space can, due to high retail rents, support relatively high land values. For redevelopment to occur, the allowable base density must support enough land value to enable a developer to buy and redevelop the property. If the combination of the value of the base density and any bonus density value not captured by an amenity contribution is still less than the value of the site in its current use, then redevelopment will not occur and the goal of densification will not be achieved. This means either being patient (i.e. waiting until redevelopment values climb due to market growth), increasing the allowable density, or accepting smaller amenity contributions.
9. Redevelopment sites must trade in the market at the value supported by the base density, so that developers can afford to obtain the bonus density by providing an amenity contribution. If developers are not aware of how the density bonus system works, they may overpay for sites (based on the potential maximum total density rather than the base density) and then complain about having to make an amenity contribution. If there has been a history of no amenity contributions at rezoning, or amenity contributions worth significantly less than the value of the density bonus, then the "un-captured" land value gain will be capitalized into site values. In this circumstance, changing the amenity contributions means that some developers will have paid too much for sites and that some landowners will be reluctant to accept the new market reality that sale price should be based on the base density, not the potential for upzoning. Also, if rezonings are readily approved outside the scope of the density bonus system, and if such rezonings do not require an amenity contribution, developers will not use the system. For the system to work, Council must be consistent in its application, developers must understand the system, and land owners must realize that their property value is based on the "old" zoning or base density, not the new maximum density in the new zoning.

2.4.2 Municipal Objectives and the "Fit" with Density Bonuses

Density bonusing is more suited to some community development aspirations than others:

- Densification. Density bonusing is well-suited to the broad goal of densification because it allows higher density, creates incentives for developers to use land more intensively, and creates a mechanism for funding or providing amenities that enhance the community.
- Revenue for area-wide amenities, such as public realm improvements or neighbourhood facilities. Density bonusing can generate revenue that can be used for area-wide community amenities if the system includes provision for cash-in-lieu instead of on-site amenities.
- On-site amenities. Density bonusing can be well-suited to the provision of on-site amenities, depending on the kinds of amenities the City wants to achieve, the typical size of development projects, and the value of additional density. If a site is only 10,000 square feet, the density

bonus allows up to 2 additional FSR, and land value is $25 per square foot of extra density, the maximum contribution is $500,000. If all-in construction cost for an amenity space (e.g. day care or community meeting space) is say $250 per square foot, the amenity contribution only yields 2,000 square feet of space. This may not be large enough to meet the amenity objective, so it may be necessary to shift to a cash-in-lieu approach to pool contributions to achieve a large community space. On the other hand, small open spaces and public art are ideal candidates for on-site amenity.

- Specific project characteristics. Some communities provide bonus density in exchange for meeting design or sustainability criteria. For example, a bonus could be earned by meeting a certain LEED standard (or equivalent) or by providing certain architectural elements (e.g. weather protection along sidewalks). There is debate as to the extent these are really community amenities; it is also possible to achieve these kinds of objectives using other tools such as Development Permits or building bylaws. Municipalities must decide whether amenities or building features are the higher priority use of potential contributions.

2.4.3 Elements That Will Help Build Acceptance in the Development Industry

The use of density bonusing is voluntary, so for the system to work developers have to want to use it. Based on our experience, developers are interested in these attributes:

- Predictability. Developers prefer a system that is simple, predictable, minimizes risk, and is administered efficiently. They lean toward the “pre-zoning” approach because this takes the rezoning risk out of the density bonus system. If the pre-zoning approach defines a specific formula for calculating amenity contribution, developers can build this amount into their financial analysis for development projects without having to wait for the outcome of a negotiation. Developers also like a system that provides density bonus without site-by-site rezoning risk.
- Consistency. Developers prefer a system in which all developers and projects are treated consistently, both because this is fair and because it contributes to predictability. This does not mean that every project pays the same dollar amount, but it means that the approach to determining amenity contribution is equitable, defendable, and consistently applied.
- No downzoning. Developers and land owners will react with great hostility to any density bonus system that starts by down-zoning property and then enables recovery of the density by making an amenity contribution. This type of down-zoning is very disruptive in the marketplace and can be argued to be fundamentally unfair to those who have made acquisitions in good faith based on existing zoning. The density bonus system should use existing density as the base or outright density and then add potential new density on top of that.

2.4.4 Ensuring Amenities Remain in Perpetuity

Once incorporated into a development, the bonus density exists “in perpetuity” or until the building is demolished. It is important, therefore, to ensure that the amenity obtained in exchange for the extra density is comparably long-lived. This means that municipalities should anticipate these issues:

- If the amenity is a capital item (e.g. an open space, a day care), it will require some form of tenure to ensure ongoing public access, such as a strata title lot in the name of the City, or long term lease, or statutory right of way. As well, a capital item also requires an operating budget, so the City must anticipate how the amenity will be maintained.
- If the amenity is on private property (e.g. a piece of public art), the City must have a means of ensuring that the amenity remains on site, is accessible, and is insured for replacement in the event of damage or theft.
- If the amenity is in the form of some kind of project characteristic (e.g. sustainability features), the City must have a means of ensuring the continued existence of these features. This can be a challenge if the sustainability features are in private units (e.g. low flush toilets) or if the features are difficult to monitor.

3.0 Key Inputs to a System for Victoria's Core Area

This section contains information and analysis regarding the Core Area that is necessary for the design of a density bonus system. This section includes:

- A review of the City's current system for granting bonus density in Downtown.
- A description of the City's objectives for community amenities.
- A description of the City's current aims for densification (i.e. the location and amount of additional density that is contemplated).
- A forecast of the total amount of development likely to occur in the Core Area and an estimate of how much of this development might involve density bonusing.
- An estimate of current Core Area land values and the implications for the potential for the amount of amenity contributions that might be obtained.
- An analysis of the economics of heritage building rehabilitation and the implications for the amount of bonus density that might have to be provided to facilitate projects.
- Overall implications for the design of a density bonus system for the Core Area.

3.1 Current System

Victoria has an existing density bonus policy for Downtown, which was adopted as part of the 1990 Downtown Victoria Plan.

The existing (1990) policy allowed for the approval of additional density, via individual site rezoning, to achieve a wide array of objectives including:

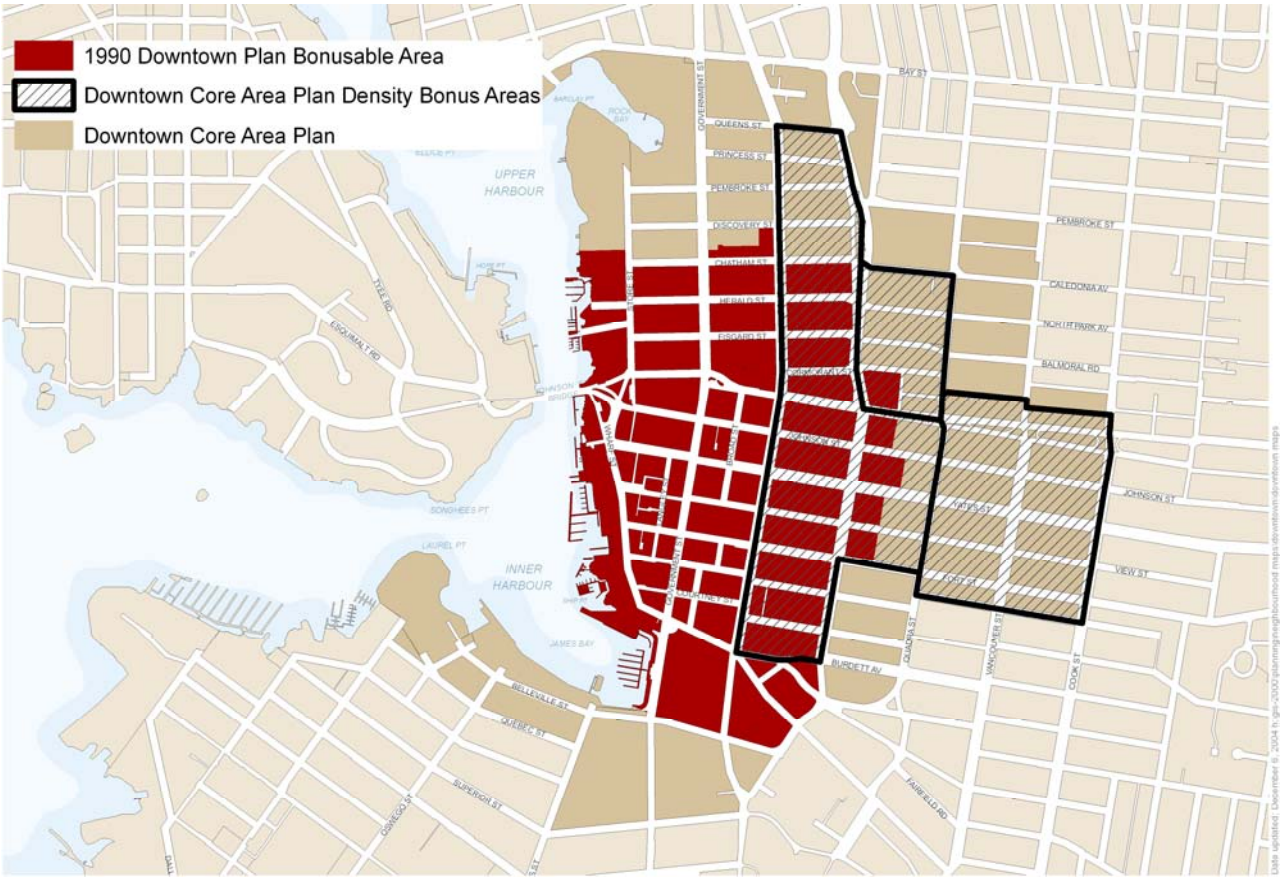
- Rehabilitation of heritage buildings.
- Development of new residential units.
- Provision of excess customer parking.
- Public realm improvements such as public open space or squares, mid-block walkways, or arcades.
- Exceptional design.
- Provision of housing or services for handicapped people.
- Community facilities such as day care.

The 1990 policy proposed a "standard entitlement" or base density of FSR 3, but various sites were assigned lower base densities for sites considered "sensitive". For example, the density of new office buildings in Old Town was limited to FSR 1 in order to encourage retention of the

existing buildings. Bonus density could be achieved above these base densities by providing amenities.

Exhibit 2A shows the 1990 Downtown Plan's designation of areas eligible for density bonusing (as well as the currently proposed expansion of the bonus area).

Exhibit 2A: Existing and Proposed Density Bonus Areas



The 1990 policy outlines some basic density bonus principles, particularly the idea that extra density may be earned by the provision of certain amenities, but it does not provide much detail to guide decisions about individual applications. For example:

- There is not a defined upper limit on the amount of additional density that can be achieved.
- There is not a prescribed basis for determining how much additional density is warranted by providing an amenity, or how much of an amenity must be provided.
- The eligible amenities cover a very broad range without any indication of priority.
- Some of the amenities are quite vague, such as "demonstrable benefit" or "exceptional design".

Because the existing policy does not provide much detail, individual projects approved under this policy show a wide variation in the amenity provided and the density achieved.

Attachment A (at the end of this document) summarizes 12 projects approved during 2004 to 2009 under the existing policy.

Based on these 12 projects and on general comments from staff about the current process, the following observations can be made about the current approach:

- Density increases have varied widely, from under 1 FSR to almost 5 FSR.
- Amenity contributions have been quite diverse and in most cases consist of a package of various benefits. Some have included cash contributions for specific purposes (for example, public art, affordable housing fund contribution, art gallery contribution), open space accessible to the public, extra underground parking, mid-block walkways, some housing units with adaptable design, some housing units being rental, streetscaping, or heritage building preservation. Note that some of these amenities are specifically listed in the existing policy but some are interpretations of the vague policy language (e.g. public art, rental housing, art gallery contribution).
- The approach to defining the amenity contribution has tended to be ad hoc, based in part on the interests of the developer, the interests or priorities of the City at the time, and the specific characteristics of the site. There has not been an overall amenity strategy for Downtown. In some cases, the "amenities" are simply desirable project characteristics that do not necessarily enhance the attractiveness of the Core Area for new residential or commercial development.
- The approach to determining the appropriate amount of amenity contribution has been ad hoc. Staff have not been using a prescribed approach to setting a target total value of contribution and the staff reports do not typically include an estimate of either the total value of the contribution or the value of the additional approved density. This is partly because some of the amenities would be difficult to monetize. This is not necessarily a problem; it simply represents a challenge in terms of deciding whether the City achieved a reasonable contribution or determining whether developers and projects have been treated consistently.
- The "take-up" has not been large in terms of number of projects, averaging about 2 proposals per year over 6 years. One of these did not proceed and one is still in the approvals process, so the pace of approvals over the past 6 years is say 1.7 projects per year. The total amount of approved density bonus floorspace is significant. The total additional floor space is not reported in all cases, but it appears that up to about 600,000 square feet of additional space was generated by density bonus, or an average of about 100,000 square feet per year. As shown in Section 3.4, we anticipate that the overall pace of Downtown development over the next couple of decades will be about 400,000 square feet per year (say 340,000 square feet of residential, or about 340 units, plus 60,000 square feet of office), suggesting that up to about 25% of new Core Area development has been density bonus floor space that makes an amenity contribution.

The existing system has produced densification in Downtown and it has generated significant amenity contributions for the City, so it has been successful. The City's aim in revamping the system is to improve it by making it more predictable (for the City, developers, and the community), more efficient, more coordinated with the planning objectives for the Core Area, and potentially more productive in terms of the total creation of amenities.

3.2 City Objectives for Community Amenities

3.2.1 Public Realm Improvements

As part of the central area planning process, the City has developed a list of priorities for public realm amenities in the Core Area.

The City's objectives include:

- Pedestrian network improvements in the public realm, including sidewalk widening, undergrounding power lines, public signage, enhanced sidewalk treatments, trees/landscaping, and pedestrian scale lighting. It will not be possible to produce area-wide upgrading by relying on individual redevelopments to make improvements along their street frontages. These improvements require a cash-in-lieu component for density bonusing, to enable the City to accumulate funds from various projects and then spend the money strategically.
- Beautification including street furniture and illumination of public buildings and structures. These require a cash-in-lieu system. These improvements may help make the Core Area a more attractive location for visitors, businesses, and possibly residents, but (arguably) it would be hard to characterize these as helping the Core Area deal with the impacts of increased density.
- Public open space improvements such as improvements to parks, plazas, water features, performance spaces, public art. These do enhance liveability and using density bonus for this purpose makes up for a major shortcoming of DCCs, which can be used to acquire park land in urbanizing areas but not to allow more intensive use of existing parkland in urbanized areas where it is difficult to buy more land for park. This requires a cash-in-lieu system.
- Transit corridor improvements such as enhanced transit stations, shelters, seating, and lighting. This requires a cash-in-lieu system.
- Acquisition of additional park land in parts of the Core Area such as Rock Bay and the proposed residential mixed use district, to meet the needs of expected growth. This park land acquisition is an allowable use of DCC funds, which could be used instead of (or in addition to) amenity contributions from density bonusing. This requires a cash-in-lieu system to pool funds as well as negotiations with individual land owners to obtain the land.

- Completion of the harbour pathway. This requires a cash-in-lieu system, except in circumstances where a waterfront site is being redeveloped, in which case the project could be required as part of rezoning to upgrade the adjacent portion of the walkway (and in which case the City may also need to negotiate for the right to create a walkway across private land).

In general, this is a public amenities and community benefits strategy that is well-suited to density bonuses, particularly with a cash-in-lieu approach. There are a couple of items on the list that, in our view, might be refined but generally these amenities are good candidates for a density bonus system that includes a cash-in-lieu component.

3.2.2 Heritage Building Rehabilitation

The City also wants to use density incentives to facilitate heritage building rehabilitation in Old Town.

In this case, bonus density is granted to the owner/developer of a heritage property to assist in the refurbishment and seismic upgrade of an important heritage building. This is not a cash-in-lieu system; the developer must upgrade the building and receives transferrable density bonus to help make the numbers work. The system requires that heritage developers are entitled to sell the transferrable density to other development sites (in designated "receiver" areas), which must be appropriately zoned or rezoned to allow the additional density to be "imported". It is very important to understand that this means there will be some Core Area sites that could potentially achieve higher density in two very different ways: obtaining bonus density by providing an amenity contribution, or acquiring transferrable heritage density. There will be an interaction in the marketplace between these two kinds of available density, so the City must design a system that manages this interaction, because of these issues:

- The City will define a target value for density provided in exchange for amenity contributions. Whether the City uses a site-by-site rezoning approach or a pre-zoning approach, there will still be a need to define a value for density and this is likely to be some percentage of current actual market value.
- Developers who hold transferrable density (granted to them to facilitate heritage rehabilitation) will want to sell this density (because the revenue from the density is a key ingredient to making the heritage project viable). The City will not be directly involved in setting the price for such transferrable density, although the City will have an indirect influence based on the pace and deemed value at which the City "creates" such density. This pace is of course determined by the number of heritage projects (with transferrable density) the City approves and the amount of density that is necessary to make any given project work financially. There will be a resulting market price for transferrable density, with this price determined by the total amount of transferrable density available for sale at any given time, the number/size of development projects looking for extra density, and the price of the density obtainable directly

from the City in exchange for amenities. The market price for transferable density will not necessarily be the prevailing market value for development sites, so there could be a difference between the value of bonus density for amenities and the value of transferable heritage density.

- If the price of transferrable density is low (too many sellers, not enough buyers), developers will prefer to buy this density rather than obtain density via amenity contributions. The City may get "too much" heritage rehabilitation and "not enough" public realm improvements in Downtown. If the price of heritage density is comparable to the value of density from amenity contributions, the mix of heritage and amenity density will be somewhat arbitrary depending on the participants in the market, unless the City regulates the mix.

There are ways to manage this challenge of overlapping bonus density opportunities.

In developing a solution, it is useful to consider the experience of the City of Vancouver, which has been operating a transferrable heritage density system for many years. We have worked with Vancouver in evaluating and refining its system. Based on this experience, we have these observations:

- It is important to monitor the pace of creating transferrable density and the pace of take-up, to know how much density is available for sale at any time. The size of this pool relative to demand has a large impact on price. The City has experienced times when the pool is very large and prices have fallen, which means that the amount of density that must be granted to make a project viable increases, further exacerbating the deflation problem.
- It is very helpful to identify mechanisms for the sale of heritage density that do not overlap with other means of acquiring density. For example, Vancouver defines receiver areas in which projects can develop up to 10% more space than allowed under existing zoning, without having to rezone, provided the extra density is acquired from the pool of transferrable heritage density. The City is considering increasing this density gain to 15%.
- It is helpful to have a public benefits strategy that allocates priority to various public goals, so that there is not constant debate over what proportion of a project's amenity contribution should take the form of heritage public realm improvements or some other amenity. In Victoria's case, this would mean that in "overlap" areas (where it is possible to acquire heritage density or bonus density via amenity contributions), the City would define a limit on the proportion of a project's increased density that can come via the heritage route.

We recommend that Victoria's system include these features:

- The City should monitor and manage the pace at which it creates transferrable heritage density bonus space. If it creates too much, the price will fall, with two bad consequences. First, developers will not want to obtain density via amenity contributions because it will be cheaper to obtain density from heritage transfers. Second, the City will have to grant increasing amounts of transferrable density to make heritage projects viable. So, it will be

essential to match the creation of transferrable density with the market's ability to take up the extra space.

- The City should consider capping the amount of transferrable heritage density a development can acquire in "overlap" areas, so that a project must obtain at least some of its density bonus by providing an amenity contribution. There should not be a minimum heritage component, because there may be times when no transferrable heritage density is available for sale.
- The City could consider allowing small density increases outside the formal density receiver areas if the extra density is transferrable heritage density.

3.3 Densification Plans

As part of the Core Area planning process, the City has identified potential areas for densification. The City has defined three areas (A, B, C) for additional density. The proposed system generally provides for a base density of FSR 3 throughout the area and a maximum FSR of 4.5 to 6 depending on the area (i.e. bonus density of 1.5 FSR to 3 FSR). The areas provide the density bonus as residential or office or mixed use. Exhibit 2B shows the density bonus areas.

Exhibit 2B: Density Bonus Areas

The City also contemplates increasing building heights to accommodate the additional density.

Note that Areas A, B, and C are areas where additional density can be developed. The Plan will also identify areas where transferrable density can be created as part of heritage rehabilitation projects.

Generally the proposed densities (base and bonus) are reasonable based on these observations:

- Development at the base density (FSR 3) already requires concrete construction. Adding the bonus density does not require a change in basic building type.
- The base density is equal to existing zoned density, so there is no down-zoning.
- The densities are broadly consistent with the actual densities achieved in rezonings involving density bonuses over the last 6 years or so in Downtown, suggesting that the higher densities are marketable and financially viable.

- The densities do not require a scale of development that is disproportionate relative to the scale of the market. As an illustration, a development on a 20,000 square foot site at FSR 3 (the proposed base density) yields a development of 60,000 square feet. If this is residential, the project would have about 60 units. Increasing density to FSR 5 yields 100,000 square feet or 100 units which is not out of keeping with the scale of recent new developments.
- By the standards of the core areas of larger cities (e.g. Vancouver, Calgary) the proposed maximum densities are low. However, Victoria's Core Area has a well-defined character that is lower scale than in larger cities and the marketplace is smaller as well. The proposed densities are in keeping with Core Area character.

In addition to the areas identified for bonus density, the City has identified "receiver" areas that are allowed to absorb transferrable bonus density that comes from heritage rehabilitation projects in Old Town. A small subset of the receiver areas is outside the boundaries of Areas A, B, and C, so in these areas the only way to achieve bonus density is to acquire transferrable heritage density. However, density bonus Areas A, B, and C are also heritage receiver areas, so in these locations development projects can obtain bonus density either by making an amenity contribution or by acquiring transferrable heritage density, or some combination. This overlap must be managed if the City wants both kinds of density opportunity to be used.

3.4 City of Victoria Downtown Demand Projections

To have some sense of the magnitude of the potential for amenity contributions, it is necessary to estimate the likely total pace of urban development in the Core Area and to estimate the proportion of new development that will be accommodated in bonus density that makes a contribution. Not all projects will use the density bonus opportunity, for various reasons, and those that do will not always use the maximum opportunity.

In early 2007, we completed detailed projections of potential demand for new residential units and new office space in Downtown Victoria. For the purpose of the forecasts, Downtown was defined to include the Downtown planning area plus the adjacent neighbourhoods of Vic West, Harris Green, Fairfield and portions of James Bay.

As input to evaluating a new density bonus system for Downtown Victoria, we reviewed the 2007 demand projections to determine whether the projections are still reasonable.

3.4.1 Residential Projections

Exhibit 3 summarizes our 2007 residential demand projections for the Downtown and fringe area. These figures exclude demand in locations near Downtown that are west of the Inner Harbour (e.g., the Songhees and Dockside areas).

Exhibit 3: Projected Multifamily Residential Unit Development in the Downtown and Fringe Area - East of Inner Harbour (Rounded)

	2006 to 2011	2011 to 2016	2016 to 2021	2021 to 2026	Total 2006 to 2026
Lower Demand Scenario (units per year)	340	340	360	330	6,850
Higher Demand Scenario (units per year)	405	405	485	515	9,050

To evaluate whether the 2007 projection is still reasonable over the long term, we:

1. Examined the most recent long range population projections and housing growth projections available for the CRD (by Urban Futures and BC Stats).
2. Analyzed recent residential development trends in the CRD by unit type (between 2007 and 2009).
3. Estimated the share of total regional apartment development that has gone to the Downtown study area over the past 2 or 3 years.
4. Updated our 2007 projection to reflect any recent changes in total expected long range regional housing demand and the share of demand that could go to Downtown.

Based on this review, we think that the 2007 "Lower Demand Scenario" is good reflection of potential future residential demand in Downtown. The "Higher Demand Scenario" is likely optimistic. Therefore, we anticipate development of about 340 apartment units per year over the next 20 years or so. Assuming an average gross floor area of 1000 per unit, this means up to about 340,000 square feet of space per year on average.

3.4.2 Office Projections

Exhibit 4 summarizes our 2007 projected office space growth in Downtown Victoria from 2006 to 2026.

Exhibit 4: Projected Downtown Victoria Office Floorspace Growth

	2006	2011	2016	2021	2026	Total Growth
Lower Demand Scenario	4,500,000	4,793,488	5,088,063	5,385,150	5,681,150	1,200,000
Higher Demand Scenario	4,500,000	5,125,038	5,547,313	5,968,025	6,367,025	1,900,000

All figures in square feet.

To evaluate whether the 2007 projection is still reasonable over the long term, we:

1. Analyzed changes in occupied office space in Downtown and in the region between 2006 and 2009.
2. Reviewed existing plans for significant office projects in Downtown and the region.

Based on our review, the 2007 projections are still a reasonable range for the expected long term office demand in Central Victoria. So, we anticipate about 60,000 square feet of new office development per year on average in the Core Area.

3.4.3 Potential for Density Bonus Space

The total estimated pace of Core Area development, therefore, is about 400,000 square feet per year. As the City's proposed density bonus figures suggest increasing from FSR 3 to a maximum of about FSR 6, for some projects the maximum share of space that is density bonus is about half. However, some of the density districts only allow a maximum of about FSR 4, so the maximum share that could be bonus space is 25%.

Based on actual approvals over the last 6 years, the City has granted about 100,000 square feet of density bonus space per year, which is equivalent to about 25% of the projected pace of development. A new system can be assumed to increase the rate of take-up of density bonus space, because a much wider array of sites will be eligible and improvements will be incorporated over the current system. However, given the proposed maximum FSRs achievable in some of the bonus areas, the fact that not all projects will use the density bonus opportunity, and the fact that some Core Area development will occur outside the designated bonus density areas, it seems reasonable to assume that the pace of density bonus take-up would likely be a maximum of about 25% of all new development, or about 100,000 square feet of space per year.

3.5 Downtown Office and Residential Land Values

To estimate the potential value of future amenity contributions, it is necessary to estimate the value of bonus density. The maximum value that can be achieved is the actual market value of the density (i.e. the land value expressed as dollars per square foot of bonus development potential), as developers will not generally pay more than the density is worth. In practice, the achievable value is less than full market value as it is helpful to leave some of the value in the project as an incentive or as money that can pay a premium for land to accelerate land purchase, site assembly, and redevelopment.

As input to evaluating a new density bonus system for the Core Area, we estimated the land value that is supportable by concrete highrise strata apartment development and high density office development in Downtown.

Our estimates rely on available sales evidence over the last few years and on land residual analysis that we completed for hypothetical high density residential and high density office projects in Downtown under current market conditions.

3.5.1 Estimated Residential Land Value

Our residential land value analysis is contained in Exhibits 5 and 6. The analysis in Exhibit 5 is representative of a hypothetical mid-quality highrise project in Downtown. Exhibit 6 assumes the project is higher quality so the revenue and construction costs are higher.

Our land residual analysis indicates that the current market value for zoned, serviced high density residential development sites in Downtown Victoria is between $30 and $40 per sq.ft. of buildable floor space. This is consistent with current listings for high density residential development sites in (or near) Downtown.

Sites in high value locations (such as on the waterfront) would have higher land values.

3.5.2 Estimated Office Land Value

Our office land value analysis is contained in Exhibits 7 and 8. These exhibits provide two different approaches to estimating the supportable land value of an office development site.

- Exhibit 7 assumes the building is constructed by a developer who sells the completed project to an investor at a premium to the total construction costs (a developer's profit margin is included the analysis).
- Exhibit 8 assumes that the developer holds the office building for the long term and requires a premium above the annual return (capitalization rate) that could be realized from acquiring an existing comparable office building, to account for the risks associated with the development process.

Based on our land residual analysis, we estimate that the current market value for zoned, serviced high density office development sites in Downtown Victoria is between $15 and $20 per sq.ft. of buildable floor space.

3.5.3 Potential for Amenity Contribution

Using the estimated land values and the estimated pace of development, we can produce a rough estimate of the potential value of future amenity contributions. Exhibit 9 below uses the low end of the estimated range of land values.

Exhibit 9: Estimated Potential for Amenity Contributions

Type of Space	Estimated Rate of Annual Growth	Share That Makes an Amenity Contribution	Value of Amenity Contribution at 75% of Land Value	Total Potential Value per year
Residential	340,000 sq. ft.	25%	$30 x 75% = $22.50 per square foot	$1.9 million
Office	60,000 sq. ft.	25%	$15 x 75% = $11.25 per square foot	$0.16 million
Total	400,000 sq.ft.			Say $2 million

The estimated total potential value of amenity contributions is in the range of $2 million. Note that is the total including any portion that takes the form of acquiring transferrable heritage density. If (for illustrative purposes) 10% of the potential is heritage related, the amenity value available to the City for other amenities is 90% of the indicated total, or about $1.7 million per year.

Given the array of amenities that the City is interested in, this level of capital funding (assuming that the City receives it all in the form of cash-in-lieu) will not go far, so it will be important to prioritize spending in order to complete some objectives, rather than making small incremental progress on all objectives at the same time.

Exhibit 5

Downtown Victoria Apartment Land Residual					
Hypothetical Concrete Apartment Development	Assumes a 15 Storey Mid-Quality Building				
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***					
Revenue and Value					
Average Sales Price Per Sq. Ft.	$475.00	per sq.ft. of net saleable residential space			
Site and Building Size					
Site size	18,000	sq.ft. or	0.41	acre	
Assumed density	5.0	FSR			
Total floorspace	90,000	sq.ft.			
Net saleable space	79,200	sq.ft. or	88.0%	of gross area	
Average Gross unit size	852				
Average Net unit size	750	sq.ft.			
Number of units	106	units or	256.52	UPA	
Required Parking Stalls	1.20	per unit			
Residential Stalls	127	stalls			
Total Stalls	127	stalls			
Construction Costs					
Allowance for Demolition of Existing Buildings	$0				
On-Site Servicing (Upgrade of Adjacent Roads/Sidewalks/Etc)	$5,000	per lineal meter of frontage			
Other Predevelopment Costs	$0				
Hard Construction Costs					
Building Costs	$180.00	per gross sq.ft. of building area			
Cost Per Parking Stall	$35,000	per parking stall			
Overall Costs Per Square Foot	$229.39	per gross sq.ft. assuming underground parking			
Soft costs (1)	10.0%	of hard costs and site prep/servicing costs			
Contingency on hard and soft costs	5.0%	of hard and soft costs			
Regional Levies	$0.00	per apartment unit			
SSAC	$0.00	per apartment unit			
DCCs	$3.330	per sq.ft. of building area			
Interim financing on construction costs	7.0%	on 50% of hard and soft costs, assuming a	2	year construction period	
Financing fees	0.5%	of hard and soft costs			
Other Costs and Allowances					
Rezoning Costs	$0				
Marketing and Commissions	5.0%	of gross revenue			
Developer's Profit	15.0%	of gross revenue, or		17.6%	of total costs
Property Taxes	0.61859%	of assessed value			
Assumed current assessment (Year 1 of analysis)	$3,000,000				
Assumed assessment after 1 year of construction (Year 2 of analysis)	$18,810,000	(50% of completed project value)			
Analysis					
Revenue					
Gross sales revenue	$37,620,000				
Less marketing and commissions	$1,881,000				
Net sales revenue	$35,739,000				
Construction Costs					
Allowance for Rezoning Costs	$0				
Allowance for Demolition of Existing Buildings	$0				
On-Site Servicing (Upgrade of Adjacent Roads/Sidewalks/Etc)	$221,893				
Other Predevelopment Costs	$0				
Hard construction costs	$20,645,000				
Soft costs	$2,064,500				
Contingency on hard and soft costs	$1,146,570				
Regional Levies	$0				
SSAC	$0				
DCCs	$299,742				
Interim financing	$1,706,439				
Financing fees/costs	$121,889				
Total construction costs	$26,206,033				
Developer's Profit	$5,643,000				
Residual to Land and Land Carry	**$3,889,967**				
Less interim financing on land (approvals/presales/construction)	$633,092				
Less property purchase tax	$63,137				
Less property taxes	$144,193				
Residual Land Value	**$3,049,544**				
Residual Value per sq.ft. of site	**$169.42**				
Residual Value per square foot buildable	**$33.88**				
Notes:					
1) Soft Costs allow for design, engineering, legal, survey, project management, consultants, permits, warranties, deficiencies, misc.					

Exhibit 6

Downtown Victoria Apartment Land Residual					
Hypothetical Concrete Apartment Development	Assumes a 15 Storey High-Quality Building				
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***					
Revenue and Value					
Average Sales Price Per Sq. Ft.	$540.00	per sq.ft. of net saleable residential space			
Site and Building Size					
Site size	18,000	sq.ft. or	0.41	acre	
Assumed density	5.0	FSR			
Total floorspace	90,000	sq.ft.			
Net saleable space	79,200	sq.ft. or	88.0%	of gross area	
Average Gross unit size	852				
Average Net unit size	750	sq.ft.			
Number of units	106	units or	256.52	UPA	
Required Parking Stalls	1.50	per unit			
Residential Stalls	159	stalls			
Total Stalls	159	stalls			
Construction Costs					
Allowance for Demolition of Existing Buildings	$0				
On-Site Servicing (Upgrade of Adjacent Roads/Sidewalks/Etc)	$5,000	per lineal meter of frontage			
Other Predevelopment Costs	$0				
Hard Construction Costs					
Building Costs	$200.00	per gross sq.ft. of building area			
Cost Per Parking Stall	$35,000	per parking stall			
Overall Costs Per Square Foot	$261.83	per gross sq.ft. assuming underground parking			
Soft costs (1)	10.0%	of hard costs and site prep/servicing costs			
Contingency on hard and soft costs	5.0%	of hard and soft costs			
Regional Levies	$0.00	per apartment unit			
SSAC	$0.00	per apartment unit			
DCCs	$3.330	per sq.ft. of building area			
Interim financing on construction costs	7.0%	on 50% of hard and soft costs, assuming a		2	year construction period
Financing fees	0.5%	of hard and soft costs			
Other Costs and Allowances					
Rezoning Costs	$0				
Marketing and Commissions	5.0%	of gross revenue			
Developer's Profit	15.0%	of gross revenue, or		17.6%	of total costs
Property Taxes	0.61859%	of assessed value			
Assumed current assessment (Year 1 of analysis)	$3,000,000				
Assumed assessment after 1 year of construction (Year 2 of analysis)	$21,384,000	(50% of completed project value)			
Analysis					
Revenue					
Gross sales revenue	$42,768,000				
Less marketing and commissions	$2,138,400				
Net sales revenue	$40,629,600				
Construction Costs					
Allowance for Rezoning Costs	$0				
Allowance for Demolition of Existing Buildings	$0				
On-Site Servicing (Upgrade of Adjacent Roads/Sidewalks/Etc)	$221,893				
Other Predevelopment Costs	$0				
Hard construction costs	$23,565,000				
Soft costs	$2,356,500				
Contingency on hard and soft costs	$1,307,170				
Regional Levies	$0				
SSAC	$0				
DCCs	$299,742				
Interim financing	$1,942,521				
Financing fees/costs	$138,752				
Total construction costs	$29,831,578				
Developer's Profit	$6,415,200				
Residual to Land and Land Carry	**$4,382,822**				
Less interim financing on land (approvals/presales/construction)	$713,304				
Less property purchase tax	$71,390				
Less property taxes	$160,116				
Residual Land Value	**$3,438,012**				
Residual Value per sq.ft. of site	**$191.00**				
Residual Value per square foot buildable	**$38.20**				
Notes:					
1) Soft Costs allow for design, engineering, legal, survey, project management, consultants, permits, warranties, deficiencies, misc.					

Exhibit 7

Residual Land Value Analysis								
Hypothetical Office Building in Downtown Victoria								
Assumes developer builds, leases, and then sells to an investor and expects a 15% profit margin on value								
Assumptions								
Site and Building Size Assumptions:								
Assumed Site Size	18,000	or	0.413	acre				
FSR	5.0							
Project Size	90,000							
Rentable Area	95%	of gross area						
Underground/structured Parking	1	stall per	500	sq.ft. of gross building area				
Total Stalls	180							
Revenue and Value Assumptions:								
Average Net Lease Rate	$32.50	per sq.ft. of rentable area assuming landlord provides fit up allowance						
Operating Costs	$15.00	per sq.ft. of rentable area						
Annual Vacancy Allowance	5.0%							
Property Management	0.0%	of lease revenue (included in operating costs)						
Structural Allowance	1.0%	of lease revenue						
Assumed Net Parking Revenue	$100.00	per stall per month						
Capitalization Rate	6.50%							
Profit Allowance	15.0%	of value						
Cost Assumptions:								
Site Servicing (sidewalks, landscaping, etc)	$5,000	per lineal metre of frontage						
Building Construction Costs (to base building - shell)	$180	per sq.ft. (Note 1)						
Parking Construction Costs	$35,000	per stall (assuming structured parking)						
Base Building Hard Construction Costs	$250	per sq.ft. buildable (including parking)						
Fit-up Allowance	$35	per rentable square foot						
Soft Costs (including project management)	15%	of hard costs						
Contingency	5%	of hard and soft costs						
Regional Levies	$0.000	per sq.ft. of building area						
Municipal DCC	$2.153	per sq.ft. of building area						
Other Contributions/Levies	$0.00	per sq.ft. of building area						
Interim Financing	7.0%	on 50% of all costs assuming a			2.0	year construction period		
Property Taxes During Development	2.29316%	applied to land value in Year 1			$1,000,000			
		applied to 50% of gross value of building in Year 2, which is:					$21,271,457	
Upfront Leasing Commissions	17%	of Year 1 revenue						
Lease-up period after construction complete	3	months, or		0.25	years			
Assumed up-front vacancy cost during lease-up	$47.50	per sq.ft. (i.e. lease revenue+operating costs) on				50%	of space during lease-up	
Analysis								
Value:								
Lease Revenue	$2,639,813							
Recovered Operating Costs	$1,218,375							
Parking Income	$216,000							
Total Gross Revenue	$4,074,188							
Less Operating Costs	$1,282,500							
Less Management	$0							
Less Structural	$26,398							
Net Operating Income	$2,765,289							
Capitalized Value	$42,542,913							
Total Value per sq.ft. buildable	**$473**							
Costs:								
Site Servicing	$228,659							
Hard Construction (including parking)	$22,500,000							
Fit-Up	$2,992,500							
Upfront Leasing Commissions	$448,768							
Upfront Vacancy Cost during Lease-up	$507,656							
Soft Costs (including project management)	$3,375,000							
Contingency	$1,293,750							
Regional Levies	$0							
Municipal DCC	$193,808							
Other Levies	$0							
Property Taxes during Development	$510,720							
Interim Financing	$2,243,560							
Total Costs Before Land and Profit	$34,294,421							
Total Costs per sq.ft. buildable	**$381**							
Profit:	$6,381,437							
Land Residual:								
Land Residual Before Holding Costs	$1,867,055							
Less interim financing on land for construction plus 6 r	$277,724							
Less property taxes during approvals	$11,466							
Less property closing costs	$15,779							
Residual Land Value	$1,562,086							
Value per sq.ft. buildable	**$17**							
Value per sq.ft. of land	**$87**							
Notes:								
(1) Hard construction costs based on information from BDC Development Consultants, Altus Group, and discussions with office developers.								
Note that hard construction costs do not include an allowance for piling or for dealing with unusual soils conditions.								

Exhibit 8

Residual Land Value Analysis								
Hypothetical Office Building in Downtown Victoria								
Assumes developer builds, leases and then holds and expects a return equivalent to 1.25 percentage point over cap rates								
Assumptions								
Site and Building Size Assumptions:								
Assumed Site Size	18,000	or	0.413	acre				
FSR	5.0							
Project Size	90,000							
Rentable Area	95%	of gross area						
Underground/structured Parking	1	stall per	500	sq.ft. of gross building area				
Total Stalls	180							
Revenue and Value Assumptions:								
Average Net Lease Rate	$32.50	per sq.ft. of rentable area assuming landlord provides fit up allowance						
Operating Costs	$15.00	per sq.ft. of rentable area						
Annual Vacancy Allowance	5.0%							
Property Management	0.0%	of lease revenue (included in operating costs)						
Structural Allowance	1.0%	of lease revenue						
Assumed Net Parking Revenue	$100.00	per stall per month						
Capitalization Rate	7.75%							
Profit Allowance	0.0%	accounted for by higher cap rate						
Cost Assumptions:								
Site Servicing (sidewalks, landscaping, etc)	$5,000	per lineal metre of frontage						
Building Construction Costs (to base building - shell)	$180	per sq.ft. (Note 1)						
Parking Construction Costs	$35,000	per stall (assuming structured parking)						
Base Building Hard Construction Costs	$250	per sq.ft. buildable (including parking)						
Fit-up Allowance	$35	per rentable square foot						
Soft Costs (including project management)	15%	of hard costs						
Contingency	5%	of hard and soft costs						
Regional Levies	$0.000	per sq.ft. of building area						
Municipal DCC	$2.153	per sq.ft. of building area						
Other Contributions/Levies	$0.00	per sq.ft. of building area						
Interim Financing	7.0%	on 50% of all costs assuming a			2.0			
Property Taxes During Development	2.29316%	applied to land value in Year 1			$1,000,000	year construction period		
		applied to 50% of gross value of building in Year 2, which is:						
Upfront Leasing Commissions	17%	of Year 1 revenue					$114,329	
Lease-up period after construction complete	3	months, or		0.25	years			
Assumed up-front vacancy cost during lease-up	$47.50	per sq.ft. (i.e. lease revenue+operating costs) on				50%	of space during lease-up	
Analysis								
Value:								
Lease Revenue	$2,639,813							
Recovered Operating Costs	$1,218,375							
Parking Income	$216,000							
Total Gross Revenue	$4,074,188							
Less Operating Costs	$1,282,500							
Less Management	$0							
Less Structural	$26,398							
Net Operating Income	$2,765,289							
Capitalized Value	$35,681,153							
Total Value per sq.ft. buildable	**$396**							
Costs:								
Site Servicing	$228,659							
Hard Construction (including parking)	$22,500,000							
Fit-Up	$2,992,500							
Upfront Leasing Commissions	$448,768							
Upfront Vacancy Cost during Lease-up	$507,656							
Soft Costs (including project management)	$3,375,000							
Contingency	$1,293,750							
Regional Levies	$0							
Municipal DCC	$193,808							
Other Levies	$0							
Property Taxes during Development	$22,932							
Interim Financing	$2,209,415							
Total Costs Before Land and Profit	$33,772,488							
Total Costs per sq.ft. buildable	**$375**							
Profit:	$0							
Land Residual:								
Land Residual Before Holding Costs	$1,908,666							
Less interim financing on land for construction plus 6 r	$283,914							
Less property taxes during approvals	$11,466							
Less property closing costs	$16,133							
Residual Land Value	$1,597,153							
Value per sq.ft. buildable	**$18**							
Value per sq.ft. of land	**$89**							
Notes:								
(1) Hard construction costs based on information from BDC Development Consultants, Altus Group, and discussions with office developers.								
Note that hard construction costs do not include an allowance for piling or for dealing with unusual soils conditions.								

3.6 Heritage Building Renovation in Downtown

One component of the proposed density bonus system is the creation of transferrable density bonuses to provide incentives for the restoration and retention of important heritage resources. The City has identified Old Town as an area in which transferrable density bonus could be created. In Old Town, many important buildings have already been rehabilitated, but many important buildings remain unrestored and the long term success of Old Town as a historic precinct depends on keeping enough buildings to create an overall image and character.

In early 2007, we completed a detailed analysis of the financial viability of rehabilitating existing heritage buildings in Old Town. The purpose of the 2007 analysis was to evaluate whether the City's incentives for heritage revitalization were likely to make rehabilitation of heritage buildings financially attractive for private developers for a significant share of the remaining heritage buildings in Old Town. In that study, we found that increasing renovation costs and the fact that many of the remaining buildings have inherent complexities that add to cost were creating a situation in which property tax forgiveness alone was not enough to make some projects viable. Some other form of incentive is also required and we suggested the City consider using transferrable density bonus, which has been very successful in other communities such as Vancouver. Therefore, Victoria is considering including a heritage density bonus component in the Core Area density bonus scheme.

As input to evaluating a new density bonus system, we completed an update of the 2007 analysis to help gauge the amount of transferable bonus floorspace that may be required to make heritage projects financially attractive.

We updated the detailed financial analysis for the two case study buildings that we analyzed in 2007:

- The Duck Block, located at 1314 to 1322 Broad Street.
- The Hamley Building, located at 602 Broughton Street.

To update the revenues and costs assumptions used in the 2007 financial analysis, we:

- Analyzed recent sales and listings for strata residential units in several heritage buildings that have recently been renovated and are subject to the property tax abatement program.
- Reviewed commercial lease rates in heritage buildings that have been renovated and compared this with heritage buildings that have not been renovated.
- Examined indicators of changes in construction costs between early 2007 and late 2009, such as the Statistics Canada construction price indices and the BDC Development Consultants' construction index for Victoria.
- Interviewed a developer who is currently active in heritage building conversions in Old Town (with at least two projects currently underway) to discuss prevailing sales prices for strata

units in converted heritage buildings, current costs of renovating and restoring heritage buildings, and the current market risks associated with heritage building renovations.

The assumed renovation and conversion plans for each case study building are based on concepts produced by Busby Perkins and Will Architects in 2007. Detailed cost estimates were also produced for each building in 2007 (which we have adjusted downward by 10% to allow for changes in costs between early 2007 and 2009).

3.6.1 Duck Block

The Duck Block is an existing 3 storey building with retail/service space at grade and a mix of commercial and residential uses on the upper floors. The entire building includes about 19,899 sq.ft. of gross floorspace and the site size is 7,260 sq.ft.

Exhibits 10 and 11 contain our updated analysis for the Duck Block. The analysis assumes that a developer would acquire the building based on its estimated existing market value as an income producing property (Exhibit 10) and then renovate the building to create 16 strata residential units on the upper floors and 5,500 sq.ft. of retail space at grade. Exhibit 11 includes all of the estimated revenues, existing heritage financial incentives, and conversion costs for the project. It also includes a developer's profit margin of 15% on costs, which would be required to make the project financially attractive and create the incentive needed for developer to proceed with the renovation. The bottom line in the exhibit calculates the additional financial incentive required to make the project financially attractive.

Exhibit 11 shows that the project is not financially attractive under current market conditions and the current heritage incentive program. The financial shortfall is about $2.6 million, or about $360 per sq.ft. of site area.

We estimate that the value of multifamily residential floorspace in Downtown Victoria is between $30 and $40 per sq.ft. buildable. Therefore, if transferable floorspace is the only additional incentive available to the project, we estimate that a bonus of about 9 to 12 FSR would be required ($360 per sq.ft. of site area / $30 to $40 per sq.ft. buildable) to make this heritage rehabilitation project financially attractive.

A transferrable bonus of FSR 9 on this site (with an area of 7,260 square feet) results in transferrable density of about 65,000 square feet. This is a large amount of space considering we have estimated that the whole Core Area might only see about 100,000 to 140,000 square feet of density bonus space taken up each year. Note that if we use the lower end of the land value range the required bonus is FSR 12, which on this site yields almost 90,000 square feet of space.

This is probably an extreme case in terms of the heritage density bonus needed for project viability. There are many factors that influence financial outcomes and it is possible that this project's economic performance could be better if some assumptions are changed (e.g. higher ground floor retail rent, smaller residential unit sizes yielding higher per square foot sales prices).

The point of this case study is simply to illustrate that some sites may need a significant transferrable density bonus to be viable.

3.6.2 Hamley Building

The Hamley Building is an existing 4 storey building with retail/service space at grade and storage on the upper floors. The entire building includes about 9,960 sq.ft. of gross floorspace and the site size is 2,878 sq.ft.

Exhibits 12, 13, and 14 contain our updated analysis for the Hamley Building. Exhibit 12 estimates the current market value of the existing building as an income producing building.

We examined two different renovation/conversion scenarios for the Hamley Building.

Exhibit 13 assumes that a developer would acquire the building based on its estimated existing market value as an income producing property and then renovate the building to create 3 large strata residential units on the upper floors and 2,275 sq.ft. of retail space at grade. Exhibit 13 shows that this residential conversion project is not financially attractive under current market conditions and the current heritage incentive program. The financial shortfall is about $1.3 million, or about $465 per sq.ft. of site area.

If transferable floorspace is the only additional incentive available to the project, we estimate that a bonus of about 11.6 to 15.5 FSR would be required ($465 per sq.ft. of site area / $30 to $40 per sq.ft. buildable) to make this heritage renovation project financially attractive.

Exhibit 14 assumes that a developer would acquire the building based on its estimated existing market value as an income producing property and renovate the building to create 7,550 sq.ft. of rentable office space on the upper floors and 2,275 sq.ft. of retail space at grade. Exhibit 14 shows that this office renovation project is not financially attractive under current market conditions and the current heritage incentive program. The financial shortfall is about $0.3 million, or about $100 per sq.ft. of site area.

If transferable residential floorspace is the only additional incentive available to the project, we estimate that a bonus of about 2.5 to 3.3 FSR would be required ($100 per sq.ft. of site area / $30 to $40 per sq.ft. buildable) to make this heritage renovation project financially attractive.

A bonus of FSR 2.5 to 3.3 on this site (with an area of 2878 square feet) yields total transferrable floor area of about 7,000 to 10,000 square feet, much smaller than the transferrable bonus needed to make the Duck Block viable.

As with the Duck Block, changes in assumptions will affect project economics and, therefore, change the size of the necessary density bonus.

Exhibit 10

Estimated Value of the Duck Block as an Income Producing Property Prior to Renovation						
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***						
Site and Building Size						
Site size	7260.0	sq.ft. or	0.167	acre		
Assumed density	2.7	FSR				
Total floorspace	19,899	sq.ft.				
Grade Level Commercial Space	6,067	sq.ft. rentable				
Upper Floor Space plus grade level vertical access/lobby	13,832					
Net Rentable Upper Floor Space (excludes vertical penetrations)	12,412	sq.ft. or	90%	of gross area upper floor area		
Revenue and Value						
Grade Level Commercial					2007 Analysis	
Average Lease Rate on Grade Level Commercial	$17.50	per sq.ft. of grade level space			$17.50	
Vacancy Allowance	5%	of gross potential revenue			5%	
Property Taxes on Grade Level Commercial	$5.00				$6.00	
Other Operating Costs on Grade Level Commercial	$4.00				$4.00	
Total Operating Costs	$9.00				$10.00	
Capitalization Rate on Commercial Income	7.0%				7.0%	
Value of Grade Level Space	$231.07	per sq.ft.			$230.36	
Upper Floor Space						
Average Lease Rate on Upper Floor Space	$10.00	per sq.ft. of upper floor space			$8.00	
Vacancy Allowance	5%	of gross potential revenue			5%	
Property Taxes Upper Floor Space	$3.00				$2.50	
Other Operating on Upper Floor Space	$4.00				$4.00	
Total Operating Costs	$7.00				$6.50	
Capitalization Rate on Upper Floor Income	7.0%				7.0%	
Value of Upper Floor Space	$130.71	per sq.ft.			$103.93	
Analysis						
Net Annual Income						
Grade Level Net Income Before Vacancy	$106,173					
Vacancy	$5,309					
Unrecoverable Operating Costs	$2,730					
Net Annual Income from Grade Level Commercial	$98,134					
Upper Floor Net Income Before Vacancy	$124,120					
Vacancy	$6,206					
Unrecoverable Operating Costs	$4,344					
Net Annual Income from Upper Floor Commercial	$113,570					
Total Net Annual Income from Property	$211,704					
Capitalized Net Annual Income at:		per sq.ft. of site	per sq.ft. of building			
7.0%	$3,024,336.07	$416.58	$151.98			
8.0%	$2,646,294.06	$364.50	$132.99			

Exhibit 11

Financial Performance of the Renovation of the Duck Block as a Residential and Retail Building With Tax Incentive Program					
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***					
Revenue and Value					
Average Sales Price Per Sq. Ft.	$465.00	per sq.ft. of net saleable residential space with tax incentive			
Average Lease Rate on Grade Level Commercial	$25.00	per sq.ft. of grade level space after renovation			
Vacancy Allowance	5%	of gross potential revenue			
Property Taxes on Grade Level Commercial	$8.10				
Municipal and School Tax Portion	$7.05				
Other Operating Costs on Grade Level Commercial	$4.00				
Total Operating Costs	$12.10				
Capitalization Rate on Commercial Income	6.5%				
Value of Commercial Space Upon Lease-Up	$356.08	per sq.ft.			
PV of Tax Savings on Grade Level Commercial for 10 years	$50.66	per sq.ft. at	6.5%	discount rate	
Site and Building Size					
Site size	7,260	sq.ft. or	0.167	acre	
Assumed density	2.747	FSR			
Total floorspace	19,940	sq.ft.			
Grade Level Commercial Space	5,500	sq.ft.			
Gross Residential Floorspace including lobby/circulation	14,440	sq.ft.			
Net Saleable Residential Space	11,950	sq.ft. or	83%	of gross area	
Average gross unit size	747	sq.ft.			
Number of units	16	units			
Construction Costs					
Hard costs	$216.00	per gross sq.ft. (includes allowance for appliances)			
Allowance for site preparation and servicing costs	$0				
Soft costs (1)	10.0%	of hard costs and site prep/servicing costs			
Contingency on hard and soft costs	5.0%	of hard and soft costs			
Contributions to City	$0.00	per apartment unit			
Residential DCC	$0.00	per sq.ft. of building area (no additional space)			
Commercial DCC	$0.00	per sq.ft. of building area (no additional space)			
Financing rate on land and construction	7.0%	on 100% of land costs and 50% of hard and soft costs			
		(assuming an 18 month construction timeframe)			
Financing fees	0.5%	of hard and soft costs			
Other Costs and Allowances					
Marketing and Commissions on Residential	5.0%	of gross revenue			
Leasing and Sales Commission on Commercial	5.0%	of value			
Property Acquisition	$3,030,880	or	$152.00	per sq.ft. of existing building	
				(see worksheet on estimated current value)	
Property Taxes During Renovation	$66,000	per year			
Analysis					
Residential Revenue					
Gross sales revenue	$5,556,750				
Less marketing and commissions	$277,838				
Net sales revenue	$5,278,913				
Commercial Value					
Value of Commercial Space Upon Lease Up	$1,958,423				
Leasing and Sales Commissions	$97,921				
Net Commercial Value	$1,860,502				
Total Net Project Revenue	$7,139,414				
Property Costs					
Acquisition	$3,030,880				
Property Transfer Tax	$58,618				
Financing Costs for 18 Months	$324,397				
Property Taxes for 18 Months	$99,000				
Total Property Costs	$3,512,895				
Construction Costs					
Hard construction costs	$4,307,040				
Allowance for site preparation and servicing costs	$0				
Soft costs	$430,704				
Contingency on hard and soft costs	$236,887				
Contributions to City	$0				
DCC's	$0				
Interim financing	$261,168				
Financing fee	$23,689				
Total construction costs	$5,259,488				
Total construction costs per sq.ft.	$264				
Revenues Less Costs	-$1,632,968				
Plus Present Value of Tax Savings on Commercial	$278,628				
Plus Building Improvement Program Funding	$50,000				
Less Target Developer's Profit (15% of costs)	$1,315,857				
Net Position	-$2,620,198				
Notes:					
1) Soft Costs allow for design, engineering, legal, survey, project management, warranties, misc.					

Exhibit 12

Estimated Value of the Hamley Building as an Income Producing Property Prior to Renovation							
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***							
Site and Building Size							
Site size	2878.0	sq.ft. or	0.066	acre			
Assumed density	3.5	FSR					
Total floorspace	9,960	sq.ft.					
Grade Level Commercial Space	2,339	sq.ft. rentable					
Retail Space with Government Frontage	1,869	sq.ft. rentable					
Retail Space with Courtney Frontage	470	sq.ft. rentable					
Upper Floor Space plus grade level vertical access and Lobby	7,621						
Net Rentable Upper Floor Space (excludes vertical penetrations)	6,885	sq.ft. or	90%	of gross area upper floor area			
Revenue and Value							
Grade Level Commercial							2007 Analysis
Lease Rate for Government Frontage	$65.00	per sq.ft. of grade level space					$65.00
Lease Rate for Courtney Frontage	$35.00	per sq.ft. of grade level space					$35.00
Average Lease Rate on Grade Level Commercial	$58.97	per sq.ft. of grade level space					$58.97
Vacancy Allowance	5%	of gross potential revenue					5%
Property Taxes on Grade Level Commercial	$18.00						$15.00
Other Operating Costs on Grade Level Commercial	$4.00						$4.00
Total Operating Costs	$22.00						$19.00
Capitalization Rate on Commercial Income	7.0%						7.0%
Value of Grade Level Space	$784.62	per sq.ft.					$786.76
Upper Floor Space							
Average Lease Rate on Upper Floor Space	$1.00	per sq.ft. of upper floor space (storage rental rate)					$1.00
Vacancy Allowance	5%	of gross potential revenue					5%
Property Taxes Upper Floor Space	$0.20						$0.50
Other Operating on Upper Floor Space	$4.00						$4.00
Total Operating Costs	$4.20						$4.50
Capitalization Rate on Upper Floor Income	7.0%						7.0%
Value of Upper Floor Space	$10.57	per sq.ft.					$10.36
Analysis							
Net Annual Income							
Grade Level Net Income Before Vacancy	$137,935						
Vacancy	$6,897						
Unrecoverable Operating Costs	$2,573						
Net Annual Income from Grade Level Commercial	$128,465						
Upper Floor Net Income Before Vacancy	$6,885						
Vacancy	$344						
Unrecoverable Operating Costs	$1,446						
Net Annual Income from Upper Floor Commercial	$5,095						
Total Net Annual Income from Property	$133,560						
Capitalized Net Annual Income at:		per sq.ft. of site	per sq.ft. of building				
7.0%	$1,908,003.57	$662.96	$191.57				
8.0%	$1,669,503.13	$580.09	$167.62				

Exhibit 13

Financial Performance of the Renovation of the Hamley Building as a Residential and Retail Building With Tax Incentive Program						
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***						
Revenue and Value						
Average Sales Price Per Sq. Ft.	$465.00	per sq.ft. of net saleable residential space with tax incentive				
Average Lease Rate on Grade Level Commercial	$75.00	per sq.ft. of grade level space after renovation				
Vacancy Allowance	5%	of gross potential revenue				
Property Taxes on Grade Level Commercial	$25.00					
Municipal and School Tax Portion	$21.75					
Other Operating Costs on Grade Level Commercial	$4.00					
Total Operating Costs	$29.00					
Capitalization Rate on Commercial Income	6.5%					
Value of Commercial Space Upon Lease-Up	$1,073.85	per sq.ft.				
PV of Tax Savings on Grade Level Commercial for 10 years	$156.36	per sq.ft. at	6.5%	discount rate		
Site and Building Size						
Site size	2,878	sq.ft. or	0.066	acre		
Assumed density	3.69	FSR				
Total floorspace	10,622	sq.ft.				
Grade Level Commercial Space	2,275	sq.ft. (including storage and washroom)				
Gross Residential Floorspace including lobby/circulation	8,347	sq.ft.				
Net Saleable Residential Space	6,050	sq.ft. or	72%	of gross area		
Average gross unit size	2017	sq.ft.				
Number of units	3	units				
Construction Costs						
Hard costs	$269.10	per gross sq.ft. (includes allowance for appliances)				
Allowance for site preparation and servicing costs	$0					
Soft costs (1)	10.0%	of hard costs and site prep/servicing costs				
Contingency on hard and soft costs	5.0%	of hard and soft costs				
Contributions to City	$0.00	per apartment unit				
Residential DCC	$0.00	per sq.ft. of building area (no additional space)				
Commercial DCC	$0.00	per sq.ft. of building area (no additional space)				
Financing rate on land and construction	7.0%	on 100% of land costs and 50% of hard and soft costs				
		(assuming an 18 month construction timeframe)				
Financing fees	0.5%	of hard and soft costs				
Other Costs and Allowances						
Marketing and Commissions on Residential	5.0%	of gross revenue				
Leasing and Sales Commission on Commercial	5.0%	of value				
Property Acquisition	$2,039,424	or	$192.00	per sq.ft. of existing building		
				(see worksheet on estimated current value)		
Property Taxes During Renovation	$50,000	per year				
Analysis						
Residential Revenue						
Gross sales revenue	$2,813,250					
Less marketing and commissions	$140,663					
Net sales revenue	$2,672,588					
Commercial Value						
Value of Commercial Space Upon Lease Up	$2,443,000					
Leasing and Sales Commissions	$122,150					
Net Commercial Value	$2,320,850					
Total Net Project Revenue	$4,993,438					
Property Costs						
Acquisition	$2,039,424					
Property Transfer Tax	$38,788					
Financing Costs for 18 Months	$218,212					
Property Taxes for 18 Months	$75,000					
Total Property Costs	$2,371,425					
Construction Costs						
Hard construction costs	$2,858,380					
Allowance for site preparation and servicing costs	$0					
Soft costs	$285,838					
Contingency on hard and soft costs	$157,211					
Contributions to City	$0					
DCC's	$0					
Interim financing	$173,325					
Financing fee	$15,721					
Total construction costs	$3,490,475					
Total construction costs per sq.ft.	$329					
Revenues Less Costs	-$868,463					
Plus Present Value of Tax Savings on Commercial	$355,712					
Plus Building Improvement Program Funding	$50,000					
Less Target Developer's Profit (15% of costs)	$879,285					
Net Position	-$1,342,035					
Notes:						
1) Soft Costs allow for design, engineering, legal, survey, project management, warranties, misc.						

Exhibit 14

Financial Performance of Office and Retail Renovation of the Hamley Building					
With Tax Incentive Program					
Major Assumptions ***(shading indicates figures that are inputs; unshaded cells are formulas)***					
Revenue and Value					
Grade Level Commercial					
Average Lease Rate on Grade Level Commercial	$75.00	per sq.ft. of grade level space			
Vacancy Allowance	5%	of gross potential revenue			
Property Taxes on Grade Level Commercial	$25.00				
Municipal and School Tax Portion	$21.75				
Other Operating Costs on Grade Level Commercial	$4.00				
Total Operating Costs	$29.00				
Capitalization Rate on Commercial Income	6.5%				
Value of Commercial Space Upon Lease-Up	$1,073.85	per sq.ft.			
PV of Tax Savings on Grade Level Commercial for 10 years	$156.36	per sq.ft. at	6.5%	discount rate	
Upper Floor Space					
Average Lease Rate on Upper Floor Commercial	$22.00	per sq.ft. of upper level space (no TIs)			
Vacancy Allowance	5%	of gross potential revenue			
Property Taxes Upper Floor Commercial	$7.00				
Municipal and School Tax Portion	$6.09				
Other Operating on Upper Floor Commercial	$4.00				
Total Operating Costs	$11.00				
Capitalization Rate on Commercial Income	6.5%				
Value of Commercial Space Upon Lease-Up	$313.08	per sq.ft.			
PV of Tax Savings on Upper Floor Commercial for 10 years	$43.78	per sq.ft. at	6.5%	discount rate	
Site and Building Size					
Site size	2,878	sq.ft. or	0.066	acre	
Assumed density	3.69	FSR			
Total floorspace	10,622	sq.ft.			
Grade Level Commercial Space (rentable)	2,275	sq.ft. (including storage and washroom)			
Gross Upper Floor Commercial Space (including lobby)	8,347				
Rentable Upper Floor Commercial Space	7,550	sq.ft. or	90%	of gross area (excludes stairs and elevator)	
Construction Costs					
Hard costs	$205.20	per gross sq.ft.			
Allowance for site preparation and servicing costs	$0				
Soft costs (1)	15.0%	of hard costs and site prep/servicing costs			
Contingency on hard and soft costs	5.0%	of hard and soft costs			
Contributions to City	$0.00	per apartment unit			
DCC	$0.00	per sq.ft. of building area (no additional space)			
Financing rate on land and construction	7.0%	on 100% of land costs and 50% of hard and soft costs			
		(assuming an 18 month construction timeframe)			
Financing fees	0.5%	of hard and soft costs			
Other Costs and Allowances					
Leasing and Sales Commission on Commercial	5.0%	of value			
Property Acquisition	$2,039,424	or	$192.00	per sq.ft. of existing building	
				(see worksheet on estimated current value)	
Property Taxes During Renovation	$50,000	per year			
Analysis					
Net Annual Income					
Grade Level Net Income Before Vacancy	$170,625.00				
Vacancy	$8,531.25				
Unrecoverable Operating Costs	$3,298.75				
Net Annual Income from Grade Level Commercial	$158,795.00				
Upper Floor Net Income Before Vacancy	$166,100.00				
Vacancy	$8,305.00				
Unrecoverable Operating Costs	$4,152.50				
Net Annual Income from Upper Floor Commercial	$153,642.50				
Total Net Annual Income from Property	$312,437.50				
Value of Commercial Space Upon Lease Up	$4,806,731				
Leasing and Sales Commissions	$240,337				
Net Commercial Value	$4,566,394				
Total Net Project Revenue	$4,566,394				
Property Costs					
Acquisition	$2,039,424				
Property Transfer Tax	$38,788				
Financing Costs for 18 Months	$218,212				
Property Taxes for 18 Months	$75,000				
Total Property Costs	$2,371,425				
Construction Costs					
Hard construction costs	$2,179,634				
Allowance for site preparation and servicing costs	$0				
Soft costs	$326,945				
Contingency on hard and soft costs	$125,329				
DCC's	$0				
Interim financing	$138,175				
Financing fee	$12,533				
Total construction costs	$2,782,617				
Total construction costs per sq.ft.	$262				
Revenues Less Costs	-$587,647				
Plus Present Value of Tax Savings on Commercial	$686,251				
Plus Building Improvement Program Funding	$50,000				
Less Target Developer's Profit (15% of costs)	$428,642				
Net Position	-$280,039				
Notes:					
1) Soft Costs allow for design, engineering, legal, survey, project management, warranties, misc.					

3.6.3 Comparing the Financial Analysis with the City Proposal

The City's draft heritage density bonus scheme suggests that the maximum density bonus available for a heritage restoration project will be 3 FSR. Our financial analysis indicates that this will be sufficient for some heritage restoration projects but not all. The City may need to reconsider this cap in some cases. In our view, the City should also consider site size in reviewing the cap, because a bonus of 3 FSR on a large site produces more floor space than a larger FSR on a smaller site. From a market impact perspective, the key issue is the total amount of transferrable floor space created in a project not the FSR calculation.

3.7 Current Market Response to Existing Density Approach

One important consideration in the design of a new density bonus system is the land market and development industry response to the existing system. Two items are of particular importance:

- Does the market show interest in accessing additional density?
- Do development properties trade at prices based on existing zoning or at prices based on anticipated upzoning?

As reviewed in Section 3.1, the development industry has demonstrated willingness to seek bonus density. While the number of projects is small, a significant amount of new floorspace has been developed as bonus density. As the new system will apply to a larger area, will be more predictable, will be more carefully designed, and will be more explicitly documented, the rate of take-up should increase as long as bonus density is priced appropriately in terms of the value of the required amenity contribution.

One key consideration in the bonus density pricing mechanism is how the land market is currently pricing development sites with regard to prospects for additional density under the existing system.

Hypothetically speaking, two different market regimes could exist in Downtown:

- Redevelopment sites could generally trade at values based on existing allowable density. In this regime, developers would be of the view that there is rezoning risk (i.e. Council may not approve the rezoning even if it offers an amenity contribution), that rezoning even if successful will cost money and time, that the amount of achievable additional density is not certain, and that the cost of any required amenity contribution will be equal to a significant portion of the gain in land value due to increased density. Therefore, developers will pay for sites based on existing zoning and will not pay values based on anticipated upzoning.
- Redevelopment sites could generally trade at values based on anticipated upzoning. In this regime, developers (and land owners) would be of the view that rezoning risk is not large, rezoning costs are not unreasonably high (or at least predictable), the amount of achievable additional density is predictable, the amount of the amenity contribution is somewhat

predictable and generally less than the value of the extra density and that, all of these factors considered, developers can afford to pay somewhat more than the value based on existing zoning. Sites may not trade at the full value based on future density, because there will be costs of rezoning and some risk, but values would be higher than supported by existing zoning.

If prevailing market conditions match the first scenario above, then there is no market impediment to implementing a new density bonus system. If prevailing market conditions match the second scenario above, some developers who recently acquired sites may have paid too much and land sellers will regard (correctly) the new system as putting downward pressure on the value of their sites. Some owners will be unwilling to sell at prices based only on the existing zoning because they will have the mindset that their value should incorporate at least some of the lift from upzoning.

In order to determine which of these scenarios best describes the current land market in Victoria, we obtained from the City detailed information about a variety of development site transactions that have occurred in Downtown over the last several years, including purchase price, zoning at the time of the sale, and allowable density after rezoning.

Based on a review of these transactions it is our opinion that:

- The land values indicated by these transactions are broadly consistent with our land value estimates (in dollars per square foot of developable area) in Section 3.5.
- Most of the transactions suggest that the sites traded based mainly on existing zoning, not anticipated increased density.
- The few transactions that involved a premium over existing zoning could signal a willingness to build in some of the value of anticipated higher density. The premium is at most about 25% of the value of subsequently added density. There could also be other explanations for the premium such as a premium to complete an assembly or prevailing super-heated market conditions in 2006 to late 2008.

The new system, therefore, should be designed with consideration to the fact that some recent development site purchases may have already incorporated some share of anticipated lift. The concern is mitigated by these factors:

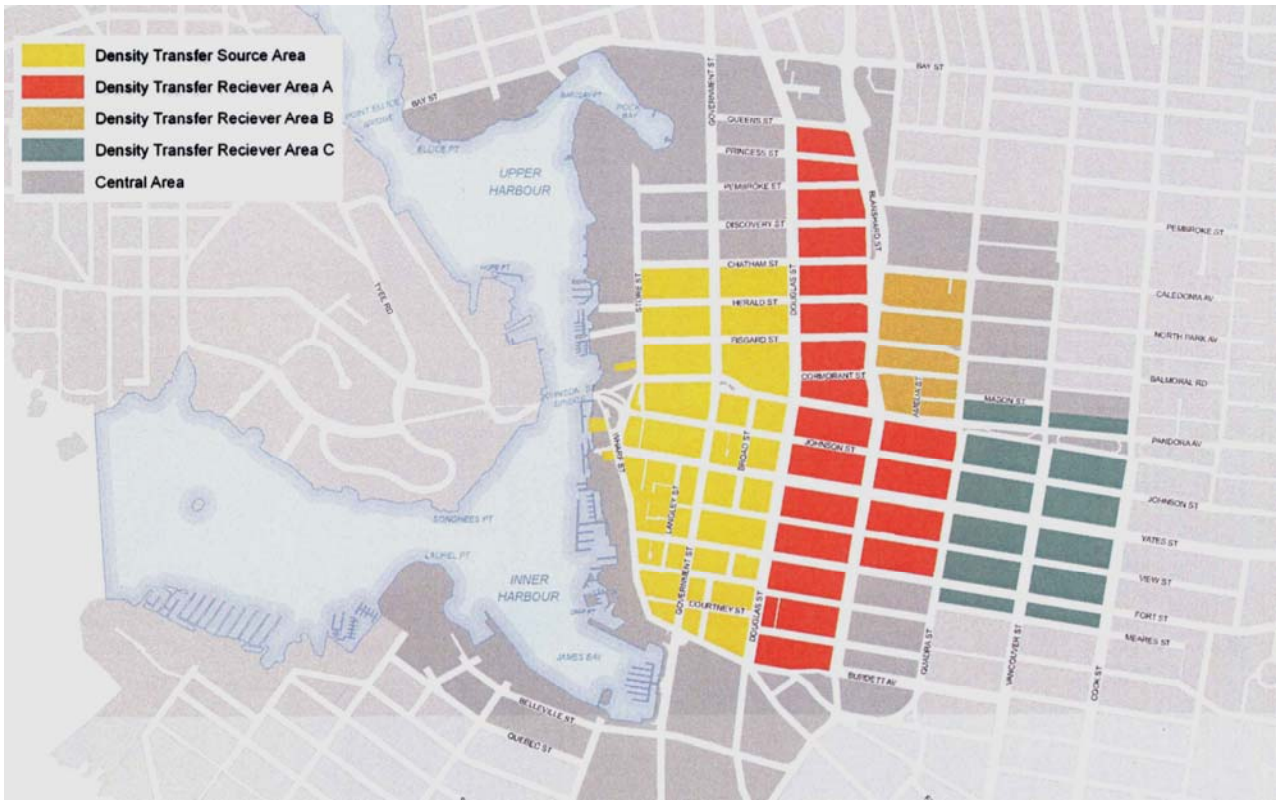
- This situation would only imply in the existing density bonus area, not the new proposed areas.
- The premium has not been paid in many cases.
- Transactions that included a premium suggest a maximum of 25% or so.

3.8 Overall Implications for Density Bonus System

Based on our analysis, the density bonus system must address these issues:

- There is a need to manage the interaction between amenity bonus and transferrable heritage bonus because there is a high degree of overlap between designated receiver areas and designated bonus areas (see Exhibit 15).
- The limit of 3 FSR on heritage source sites will be too low for some properties.
- The City's amenity priorities are highly suited to density bonusing, but require that most or all contributions are cash-in-lieu.
- The potential annual revenue generation is not large enough to implement all amenity priorities at once. The City will have to prioritize and phase its capital investments, unless it intends to borrow the capital and repay it with amenity contribution cash.

Exhibit 15



4.0 Suggestions For Proposed Density Bonus System

4.1 Assumptions

Our suggestions are based on these assumptions:

- The City's policies regarding the locations of density bonus areas, base density, and maximum density will be adopted in the Downtown Core Area Plan as an OCP bylaw.
- The City's amenity priorities will be adopted as part of the new OCP bylaw.
- The City will establish systems for collecting and allocating cash-in-lieu contributions.

4.2 Waterfront Sites

Waterfront sites are excluded from the City's designated density bonus areas. We agree with this decision because the rezoning and redevelopment of waterfront lands will require site-specific approaches to:

- Achieve on-site amenities such as public access along the harbour and public walkways.
- Deal with design so as to protect water views and waterfront access.
- Produce developments that live up to the outstanding potential of these lands.

Waterfront properties should provide amenity contributions, but these should be determined on a site-by-site basis.

4.3 Source Sites in Old Town for Transferrable Density Bonus

Heritage sites seeking transferrable heritage density bonus will have to be negotiated on a site-by-site basis, for these reasons:

- The size of the bonus cannot be determined in advance because the amount depends heavily on individual project economics.
- The bonus must be associated with a commitment (and an acceptable concept plan) for heritage restoration.

Therefore, each case will be individually negotiated.

This is not a problem, as the City already individually negotiates the provisions for property tax abatement, which requires the same kind of financial analysis that will be needed to calculate the appropriate heritage density bonus.

We suggest these refinements:

- The City should revisit the proposed cap of 3 FSR for transferrable density. Some buildings may require more bonus to be viable. If there is a cap for individual projects, it might be better to have a cap on total bonus square footage from any project rather than a cap on FSR.
- The policy should make it clear that a financial analysis must be provided in support of the application for transferrable bonus.
- The policy should make it clear that transferrable density can be used for any uses allowable at the receiver site but that in calculating the initial bonus amount the City will assume the use and value are based on the higher of residential or office land values at the time.
- The policy should require that density bonus is only available if the project has also obtained property tax abatement, to minimize the amount of the required bonus.

To implement this transferrable system, the City must:

- Clearly identify eligible receiver areas.
- Put in place a system to monitor and manage the creation and take-up of transferrable density and watch for any signs of over-supply (which would lead to a deflation in value). One approach to managing the creation of new transferrable density is to set an annual cap. A cap might avoid creating "too much" density, such that the market price falls, but there are some problems with defining a cap. First, until the system has been operating for a while it would be difficult to select an appropriate cap. The conservative approach would be to set the cap arbitrarily low, but this might inhibit desirable projects that need more density. Second, the existence of a cap could lead to a situation in which the City uses up the cap and then has no ability to approve a highly desirable application that is received afterward. We suggest setting an initial target, not to be exceeded unless there is a compelling reason, and a very careful approach to monitoring. The amount of the initial annual target will depend on whether the City's approved system includes our suggestions for expanded receiver areas (see Section 4.4) and our suggestion for a limit on the maximum heritage share of density bonus in the "overlapping" amenity areas (see last two paragraphs of Section 4.5).
- Create an education plan targeted at heritage property owners, property owners in the receiver areas, and developers.
- Maintain an easily-accessed record of who has transferrable density for sale.
- Establish the legal tools to create the transferrable density at a source site and then shift it to receiver sites.

4.4 Receiver Sites Outside of Areas A, B, and C

Receiver sites outside of Areas A, B, and C should be pre-zoned to allow them to "import" extra density.

These receiver sites need a base and maximum density defined in bylaws. Receiver sites should not be rezoned site-by-site because the marketability of the transferrable density would be impaired by rezoning risk.

The City may want to consider expanding this area, because the total amount of land outside A, B, and C is small. One way to expand the receiver areas without dramatic impact on receiver neighbourhoods is to change zoning in a larger area to allow a small increment in FSR (say 10%) without rezoning if the increment is for a heritage transfer. Vancouver uses this approach and it accounts for a meaningful share of the heritage density take-up. Vancouver is considering increasing this density top-up to 15% of FSR, but we suggest Victoria start with 10% and monitor the outcome (in terms of urban design, view impacts, architectural character) before considering a larger increment.

4.5 Areas A, B, and C

We see three alternative approaches to these areas:

3. Site-by-site. The City could rezone these properties individually on application. This means individual negotiations and continued rezoning risk, but the approach is still dramatically better than the current approach, because the base and bonus density (and height and use) will be established in the Plan, as will the amenity priorities and the emphasis on cash-in-lieu. If Council consistently approves rezoning based on OCP policy, this will work. The new approach will not be ad hoc. Because of the heritage transfer system, the City will need the capability (internal or consultants) to do the financial analysis anyway. As well, it is important to note that the total number of projects will not be large (likely 2 or 3 per year based on recent experience), so the total administrative load is not large.

4. Pre-zone. Areas A, B, and C could be prezoned to allow the base and bonus density. The pre-zoning approach will require that the bylaw defines the amenity contributions, which should be initially set at $15 per square foot of office and $30 per square foot of residential, less 25%.[3]

   These values are at the low end of the range of current market value to maximize take-up. To implement this system, the City will need a mechanism to periodically update the dollar rates in the bylaw (at least annually) based on market conditions.

   This approach eliminates political risk and eases administration. The downside is the loss of the ability to tailor site-specific amenity contributions.

5. Pre-zone, but with a developer option to apply to rezone. To maintain some flexibility for some sites, say those with some unique amenity opportunity, the City could adopt a hybrid approach along these lines:

[3] The 25% is intended to make some of the land lift available for assembly, transaction costs, and incentive.

- Pre-zone Areas A, B, and C to allow the base densities and bonus densities as proposed above.
- Identify areas where additional density (FSR 1?) could be available via rezoning under special circumstances on application by the developer (which may come about at the suggestion of the City). In these cases, a site-specific rezoning would determine the density and the amenity contributions.

Note that in this approach the developer has the certainty of the pre-zoned approach as a fall-back plus the opportunity to obtain more density.

In our view, any of these three approaches would be better than the existing approach and any could be implemented successfully. We lean toward option 3 because of its combination of reduced zoning risk while maintaining some flexibility.

In any approach, the City must address the issue of the mix between heritage and amenity bonus.

In order to ensure a market for heritage density but also to ensure that some amenity contribution is obtained, we suggest that the bonus zone include a cap on the share that can be transferrable heritage density. There should not be a minimum because there may not be heritage density for sale all the time.

We suggest an initial cap of 25% for heritage, but this should be monitored and if necessary adjusted depending on how much heritage density is being created and how much unsold heritage density there is.

4.6 Transition Policy

In new density bonus areas not in the current Plan, there is no need for a transition policy (other than a plan to communicate the new system) because the market should not have been pricing in premiums based on upzoning. However, there may be a need for a transition policy in the existing density bonus area where, as noted in Section 3.7, it appears that some (but not most) land sales in recent years have included a premium based on anticipated upzoning. This is a predictable result of the existing density bonus system.

Introducing a new density bonus system in the existing density bonus area means that it is possible that some land owners will have expectations of values being higher than supported by existing zoning and some developers may have “overpaid” for redevelopment sites. To ease the introduction of the new system, the City could consider these transitional options:

- While we suggest pricing density bonus at 75% of market value in new areas, the City could (for an interim period of say 2 years) price bonus density at a lower rate (say 50%) in the existing density bonus area. This provides an extra cushion for developers who recently bought sites under the old regime.

- The City could adopt a two-tiered bonus in the existing amenity area based on the fact that few sites have achieved density over about 5.5 FSR. Bonus density to reach 5.5 could be priced at 50% and density above 5.5 could be priced at 75%, for an interim period.

Attachment A

Rezonings Involving Density Bonus in Downtown Victoria (2004-2009)

Property Address/ Rezoning Date	FSR Lift	Additional Floor Area Achieved (m^2)	Amenity Provided
737 Humbolt December 1, 2004	Base 3.0 Bonus 1.1 Total 4.1	5,687 HR Residential	• Proposed residential use rather than office use yields 1.1:1 bonus. • Provided roof-top garden on 6th floor.
760 Johnson November 4, 2005	Base 3.0 Bonus 3.06 Total 6.06	4,095 HR Residential with ground floor commercial	• Ground floor restaurant or retail, residential tower (min 3700 m^2). • Landscaped open space accessible to public. • u/g parking.
813 – 834 Douglas January 20, 2006	Base 3.0 Bonus 2.5 Total 5.5	4,510 Commercial and Residential	• Ground floor restaurant or retail, residential tower (min 10,000 m^2). • Landscaped open space accessible to public. • $150,000 to City Housing Reserve Trust Fund. • $150,000 public art contribution. • $150,000 Contribution to Victoria Art Gallery (which will generate matching grant from Fed or Prov.)
755 Caledonia Avenue July 14, 2006	Base 3.0 Bonus 1.85 Total 4.85	13,265 Commercial Office (17,000 m^2), and 84 residential DUs	• inclusion of residential generates bonus of 1.1:1. • .75:1 bonus is attributed to: extra 355 u/g parking stalls; public open space; mid-block walkway; revitalization of north Downtown; $1000/DU contribution to Victoria Housing Trust Fund; $30,000 public art; 10% of DUs to be adaptable/accessible housing.
734 – 736 Broughton Street March 5, 2007	Base 3.0 Bonus 0.3 Total 3.3	292 4th floor addition to existing office	• On-site storage for 17 bicycles. • Introduction of glazed storefront for coffee shop use fronting on existing mid-block walkway.
1701 Douglas Street March, 2007			
1620 Blanshard (at Fisgard) April 5, 2007	Base 3.0 Bonus 4.6 Total 7.6	8,094.7 Office with ground floor restaurant/retail.	• $100,000 contribution to Housing Trust Fund. • $350,000 public art in the form of green living wall in LEED bldg. • Public open space and street-scaping at intersection. • Mid-block walkway system expansion potential. • Revitalizing investment in north Downtown.

Property Address/ Rezoning Date	FSR Lift	Additional Floor Area Achieved (m^2)	Amenity Provided
819 Yates Street May 25, 2007	Base 3.0 Bonus 2.83 Total 5.83	7,444 HR 204 unit residential with ground floor commercial	• $200,000 public art. • 10% adaptable DUs (20) • 2 DUs managed as supported housing. • public access to mid-block walkway during daylight business hours.
834 Johnson Street September 6, 2007	Base* 2.5-3.0 Bonus 3.26-2.76 Total 5.76 * Base FSR depends on site coverage.	m^2 not provided. 93 Res DUs with live/work TH at ground level.	• 50% of units to be adaptable/ accessible. • 100% of units to be capable of being rented.
800 Yates & 1321 Blanshard December 4, 2007	Base 3.0 Bonus 1.96 Total 4.96	7,870 Office with ground floor commercial/ retail.	• 175 u/g parking stalls. • Street-scaping along streets and intersection. • Revitalizing investment in north Downtown. • LEED green features including green roof and storm water bioswales. • Partial u/g power on Yates.
924 Douglas & 680 Courtney Street January 27, 2009 REZONING DECLINED	Base 3.0 Bonus 0.6-3.88 Total 3.6 over consolidated site, 6.88 if Courtney site only	1,085 Office with ground floor commercial/ retail	• Ongoing preservation of the existing cathedral at 924 Douglas (in the form of a Heritage Revitalization Agreement)
726 – 746 Yates June 3, 2009 REZONING IN PROCESS (note: rezoned in 2005 from CA-4 with FSR 3.0 to CA-51 with FSR 5.8…project did not proceed)	Original Base 3.0 2005 Rezone Bonus 2.8 Additional Bonus requested .58 Total 6.38	1,126 Office with ground floor commercial/ retail and u/g parking. (Note: total additional floor area including 2005 rezone is 6522.9 m)	• Public walkway secured by ROW. • Landscaped public open areas (min 50 m^2). • Restaurant or retail fronting Yates and walkway. • Conservation of façade at 738-740 Yates. • 149 u/g parking stalls.