



CITY OF VANCOUVER
INTERNAL AUDIT REPORT
Development Cost Levy Waiver Audit

Distribution:

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KPMG

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EXECUTIVE SUMMARY

February 9, 2017

The Development Cost Levy (DCL) Waiver audit was initiated to provide reasonable independent assurance that DCL waivers granted for affordable market rental housing since 2009 were in compliance with applicable City policies and criteria, and that business processes and related internal controls were adequate and effective.

One of the recommendations of the December 8, 2016 report by the City's Chief Risk Officer, "Review of DCL Waiver Issue for the Charleson Project," was for an internal audit of the remaining 29 DCL waivers issued since 2009. To provide 100% coverage of all DCL waivers granted, we reviewed the 29 as well as the Charleson project.

Review of the DCL waivers revealed the following:

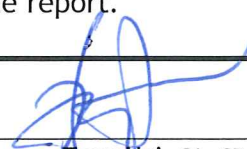
- All 29 projects were verified to have met the criteria for the DCL waiver.
- For one project which met all waiver criteria, the calculation of the DCL waiver amount may be incorrect as there was a discrepancy in the square footage used in the calculation. The discrepancy was 254 square feet and the waiver amount was \$1,394 higher. Management has committed to follow-up and correct this issue.
- The waiver relating to the Charleson Project was confirmed as an exception, in line with the Chief Risk Officer's report's findings. The waived amount has since been repaid to the City.

To effectively manage the DCL waiver process, the City needs to establish clear ownership and responsibilities, as well as formalize the business process. Management approval processes and documentation of waiver criteria should also be strengthened.

The following key process-related findings were noted:

- F.1: There is a need to establish governance and accountability over the DCL waiver process;
- F.2: A management approval process should be implemented for DCLs and DCL waiver calculations;
- F.3, F.4, F.5: Improvements are required in the retention of supporting documentation for waiver criteria.

Management has committed to address these findings. Recommendations and management action items are contained in the report.



Tony Hui, CA, CPA, CRMA
Chief of Internal Audit

A. BACKGROUND

Development Cost Levies (DCLs)

The City of Vancouver charges development cost levies (DCLs) to property developers for new developments. Revenue generated from DCLs fund City facilities such as parks, childcare, engineering infrastructure and social housing. There are City-wide and Area Specific DCLs, which are governed by DCL by-laws outlining boundaries and rates charged for each area.

DCL Waivers

Waivers or reductions of DCLs may be granted for developments that fall under certain categories such as heritage revitalization, social housing, and affordable market rental housing. DCLs can be waived for affordable market rental housing subject to meeting DCL by-law conditions for eligibility. Since 2009, DCL waivers have provided a financial incentive for developers to increase the number of affordable rental units in the market through the following programs:

- Short Term Incentives for Rental (STIR) Program (June 2009 to December 2011);
- Secured Market Rental Housing Policy, now referred to as the Rental 100 program (May 2012 - current).

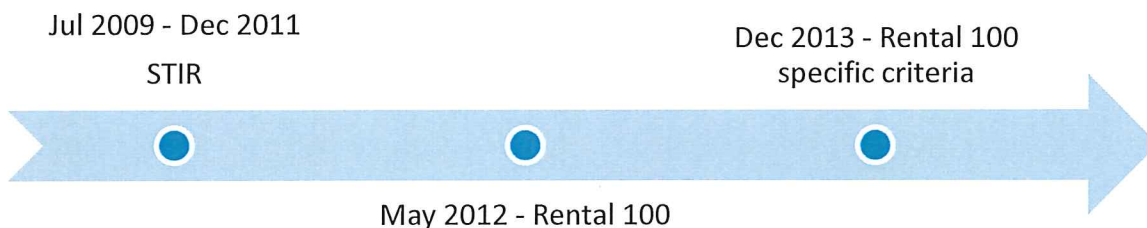
STIR program

Previously under the STIR program, mixed-use development projects that included residential strata units and affordable market rental units could be eligible for a DCL waiver for the rental portion only.

Rental 100 program

Under the current Rental 100 program, development projects must be comprised of 100 % for-profit affordable market rental units in order to qualify for a DCL waiver. Buildings with residential strata units for sale do not qualify. Council enacted specific criteria in December 2013 to determine whether Rental 100 development projects are eligible for the DCL waiver.

Timeline of Affordable Market Rental Housing Programs



Rental 100 waiver criteria

1. All dwelling units in the building are rental units;
2. Average size of rental unit not to exceed a specified square footage;
3. Average monthly rental rate not to exceed a maximum dollar amount at initial occupancy;
4. Proposed construction cost per square meter of rental area not to exceed a maximum dollar amount; and
5. The tenure of the rental is the longer of the life of the building or 60 years, or another term agreed to by the City and owner.

The above limits for the rental rates and construction costs are adjusted annually to reflect current costs. Since the inception of the DCL waiver program for affordable market rental housing, there have been 30 development projects completed where the DCL was partially or fully waived. The total value of DCL waivers granted is \$19.2 million.

Departments involved in Rental 100 projects waivers

There are three key departments involved in the process for DCL waivers relating to Rental 100 projects:

- Planning, Urban Design & Sustainability - Prepares rezoning reports for Council approval;
- Community Services - The Housing Policy group works with Legal Services to finalize a housing agreement outlining waiver conditions and verifies at the time of building permit issuance that the project qualifies for DCL waiver; and
- Development, Buildings & Licensing (referred to in this report as 'Development Services') - Performs technical reviews of projects, issues development and building permits and calculates DCLs and associated waivers.

Charleson Project

Media reports in December 2016 identified "the Charleson" as a project which erroneously was granted a DCL waiver of approximately \$1.5 million. On December 8, 2016, the City's Chief Risk Officer issued an initial report, "Review of DCL Waiver Issue for the Charleson Project". As part of the City's review of the processes relating to this incident, Internal Audit was directed to review the remaining 29 DCL waivers granted since the inception of the STIR program to ensure their validity and compliance with applicable policy.

B. AUDIT OBJECTIVES AND SCOPE

To provide 100% coverage of all DCL waivers granted since the inception of the affordable market rental housing incentive programs, the waiver criteria for all 30 projects, including the Charleson project, were reviewed. The objective of the DCL Waiver audit was to provide reasonable independent assurance over the following:

- DCL waivers for the affordable market rental housing projects granted since 2009 were in compliance with applicable City policies and criteria at the time of project approval;
- DCL waivers were appropriately authorized; and
- Related business processes and internal controls supporting DCL waivers are effective and efficient.

The audit does not include a review of DCL exemptions and DCL reductions issued by the City other than those for affordable market rental housing programs.

Our work included:

- Interviews with key staff and management in Planning, Urban Design & Sustainability, Development, Buildings & Licensing, Community Services, and Legal Services;
- Review of relevant supporting documentation including DCL bylaws, housing agreements, rezoning reports, and other departmental records and correspondence; and
- Recalculation of DCL waiver amounts.

C. ACKNOWLEDGEMENT

We would like to thank management and staff from the following departments for their cooperation and assistance:

- Planning, Urban Design & Sustainability;
- Development, Buildings & Licensing;
- Community Services - Housing Policy; and
- Legal Services.

D. CONCLUSION

All 29 DCL waiver projects reviewed were found to have been appropriately authorized, and met applicable City policies and waiver criteria. In addition, the waiver relating to the Charleson Project was confirmed as an exception, in line with the Chief Risk Officer's report's findings. The waived amount has since been repaid to the City.

To effectively manage the DCL waiver process, the City needs to establish clear ownership and responsibilities, as well as formalize the business process. Management approval processes and documentation of waiver criteria should also be strengthened. Findings and recommendations have been discussed with appropriate management and responses incorporated in this report.

E. DCL WAIVER COMPLIANCE

The DCL waiver projects were reviewed and supporting documentation obtained to verify compliance with waiver criteria. The waiver amount granted was also verified. Review of the DCL waivers revealed the following:

- All 29 projects were verified to have met the criteria for the DCL waiver.
- For one project which met all waiver criteria, the calculation of the DCL waiver amount may be incorrect as there was a discrepancy in the square footage used in the calculation. The discrepancy was 254 square feet and the waiver amount was \$1,394 higher. Management has committed to follow-up and correct this issue.
- For eight projects, there was no documentation of review of projected construction cost at the time of the waiver. Subsequent analysis showed that these projects met the waiver criteria.
- For two projects there was no documentation available to show they met the rental rate criteria at the time of granting the waiver. Subsequent information obtained revealed the rates to be within the limits for the waiver criteria.

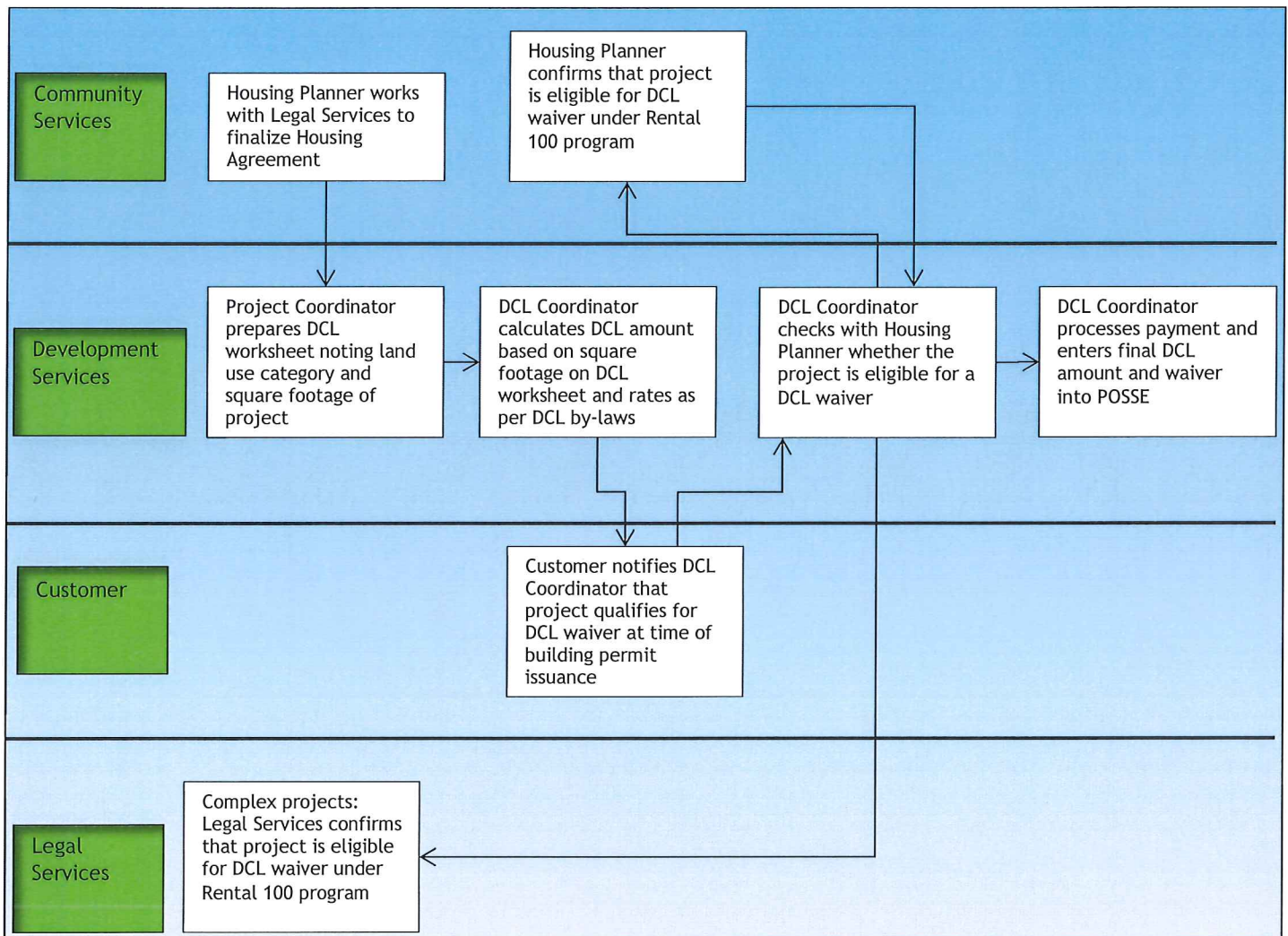
- The waiver relating to the Charleson Project was confirmed as an exception, in line with the Chief Risk Officer's report's findings. The waived amount has since been repaid to the City.

Appendix A contains the list of projects reviewed and any related exceptions.

F. AUDIT ISSUES, RECOMMENDATIONS AND MANAGEMENT RESPONSES

F.1 Establish governance and accountability over DCL waiver process

The process for calculating the DCL amount and any applicable waiver is outlined below:



- A Project Coordinator in Development Services sends a DCL worksheet to the DCL Coordinator in Development Services, noting the floor area square footage for each category of building use such as residential rental, strata, social housing, and commercial.
- The DCL Coordinator emails a Housing Planner in the Community Services department to determine whether the building meets the requirements under the Rental 100 program (and previously STIR). More complex projects are referred to Legal for confirmation of the waiver.

- The DCL Coordinator calculates the waiver based on rental square footage and enters the information into the POSSE system for tracking.

There are various staff and departments involved in the process and there is a need for clarity around where ultimate responsibility resides for DCL waivers. A DARCI (Decider, Accountable, Responsible, Consulted, Informed) Accountability Matrix is a tool that could be used to establish an effective and efficient governance structure for this process. A proposed DARCI Matrix is outlined in Appendix B.

As the Planning, Urban Design & Sustainability Department oversees new developments and associated rezoning applications, it may be practical to designate this area with overall responsibility.

Recommendation:

F.1.1 The General Manager, Planning, Urban Design & Sustainability, should assume the overall responsibility as the process owner for DCL waivers to enhance coordination and establish accountability. This should be in place by April 30th, 2017.

Management Response:

Please check one:

☒ Agree with the findings

☐ Disagree with the findings

Please check one:

☒ Agree with the recommendation

☐ Disagree with the recommendation

Management Comment:

F.1.1 - To enhance coordination and establish accountability, the General Manager of Planning, Urban Design and Sustainability will assume overall responsibility as the process owner for DCL Waivers. Following the review and approval by the Director of Housing and Projects and the Director of Planning, the General Manager of Planning, Urban Design and Sustainability or designate will sign the DCL waiver request form confirming the DCL waiver is granted, pending continued compliance.

F.2 Establish management review and approval process for DCLs and DCL waiver calculations

There is currently no review by management to ensure that the DCL and associated waiver, if applicable, are calculated correctly.

For one of the projects reviewed, the square footage used in the DCL waiver amount calculation did not match the square footage in the permitting system by 254 square feet. This resulted in a waiver that was potentially \$1,394 higher. Management indicated that they will correct this issue.

The total annual value of DCL's collected is \$51.8 million, based on a 10 year average from 2006-2015. As the process is manual, involves a high volume of transactions, and can be significant in value, establishing a practical management approval process would provide oversight and minimize the risk of calculation errors made. A checklist to document review and signoff at the various stages in the workflow would assist staff from the various departments involved.

Recommendation:

F.2.1 The General Manager, Development, Building & Licensing should ensure that all DCL waivers requested are reviewed by management for accuracy and proper documentation. To facilitate the review process a checklist should be developed highlighting the key controls and documenting management sign-off. This should be in place by May 31st, 2017.

F.2.2 The General Manager, Development, Building & Licensing should establish a business process for management review of DCL calculations, in light of the significant transaction volume and dollar value involved. A materiality threshold should be established to focus reviews on high value transactions. Spot checks on all DCL's should also be conducted, as practical. This should be implemented by May 31st, 2017.

F.2.3 The General Manager, Development, Building & Licensing should ensure that the discrepancy in the waiver amount for the one project noted is reviewed and corrected. This should be completed by May 31st, 2017.

Management Response:

Please check one:

☒ Agree with the findings

☐ Disagree with the findings

Please check one:

☒ Agree with the recommendation

☐ Disagree with the recommendation

Management Comments:

F.2.1 - A checklist has been created and is operational. As part of the new process the Assistant Director of Development will review all DCL waivers for accuracy and proper documentation, including the newly created checklist, are complete and signed off accordingly prior to being forwarded to DCL Clerk.

F.2.2 - The Assistant Director of Development will review all DCL worksheets as part of the sign off for Development Applications, so all applications of all values will be reviewed by a senior member of the Development team. Staff from other teams will also serve a cross checking function as part of the revised checklist process.

F.2.3 - The Assistant Director of Development has reviewed and accounted for the 254 square foot variance identified during the audit of one of the 30 waiver projects. The project has been reviewed, and the waiver amount was deemed to be correct. This is now complete.

F.3 Formalize process to include verification of construction cost criteria

As per the Vancouver Development Cost Levy Bylaw 9755, one of the criteria to be eligible for a DCL waiver under for-profit-affordable rental housing is that "the proposed construction cost for the rental residential area do not exceed \$2,691 per square meter, except that such costs shall be adjusted annually on January 1 to reflect any change in medium level construction costs for Residential Apartments as set out by Altus Group in the Construction Guide published in the previous calendar year".

For eight of the projects reviewed, no supporting documentation was found to support that this criterion was reviewed prior to granting the DCL waiver. Staff from the Housing Policy

department indicated that review of construction cost was not initially embedded in the review process when the Rental 100 program was first implemented. Housing Policy worked with Real Estate Services to recalculate the average construction costs. Based on these calculations, the all eight projects met the DCL waiver criteria.

Recommendation:

F.3.1 The General Manager, Development, Building & Licensing should formalize the business process to ensure that proposed construction costs for Rental 100 projects are reviewed and do not exceed the established thresholds in the DCL by-laws. This review should be documented and retained for future reference. This should be completed by June 30th, 2017.

Management Response:

Please check one:

☒ Agree with the findings

☐ Disagree with the findings

Please check one:

☒ Agree with the recommendation

☐ Disagree with the recommendation

Management Comment:

F.3.1 - The Development Services, Housing, and Planning teams have revised and formalized the DCL process to ensure there are two stages at which the construction cost is reviewed and aligns with the bylaw. This revised process has been communicated to all relevant staff and formal training will take place by April 15th.

F.4 Formalize process for reviewing rental rate criteria

One of the criteria for DCL waivers is that the average monthly rental rate is not to exceed a maximum dollar amount at initial occupancy.

Review of this criterion at the time of waiver application is necessary to determine waiver eligibility; approval by the Housing or Legal department includes a review of projected rents at that stage of the process. Staff indicated that the process has recently been revised to include review of this criterion at the occupancy stage, which more closely reflects the language of the bylaw.

For two projects there was no evidence of review of the rental rate criteria at the time of granting the waiver. These projects are not yet at the occupancy stage and rental rates were subsequently obtained by the Housing Department. Our review has shown these rates to be within the allowable limit for the waiver criteria.

The process needs to be clarified to ensure that rental rates are reviewed both at waiver application and at the occupancy stage. As a situation may arise where rates at occupancy are no longer in compliance with the waiver criteria, a process will need to be established to revoke any waivers that are found to be no longer valid.

Recommendation:

F.4.1 The General Manager, Community Services should formalize the business process to ensure that proposed average monthly rental rates for Rental 100 projects are reviewed and

do not exceed the established thresholds in the DCL by-laws. This review should take place at both waiver application and shortly before initial occupancy and should be documented and retained for future reference. A process to handle any revocation of waivers no longer valid should also be established. This should be completed by June 30th, 2017.

Management Response:

Please check one:

☒ Agree with the findings

☐ Disagree with the findings

Please check one:

☒ Agree with the recommendation

☐ Disagree with the recommendation

F.5 Ensure proper supporting documentation is retained and accessible

DCL waiver supporting documents

Supporting documentation for DCL waivers include the signed housing agreement which outlines some of the waiver criteria required in order to qualify for a DCL waiver. However, not all of the waiver criteria are included in the housing agreements, such as square footage of the rental portion (for STIR projects) and construction cost criteria (for Rental 100 projects).

Verification of DCL waiver criteria

The housing agreements are retained and stored by Legal Services and the Housing Policy department. These supporting documents are not provided or accessible to the DCL Coordinator prior to the DCL waiver calculation. In addition, the DCL coordinator is not formally notified of any potential DCL waivers prior to calculating the DCL. This is usually only flagged by the developer during the permit payment process.

Without supporting documentation being provided prior to the DCL waiver being calculated, there is a lack of ability to verify whether individual projects meet the waiver criteria before the waiver is granted. Accessibility of supporting documentation in a central document repository such as VanDocs would facilitate a process for appropriate verification of waiver criteria being met.

Recommendation:

F.5.1 The General Manager, Community Services should ensure all DCL waiver criteria for Rental 100 projects are documented and other supporting documentation for DCL waivers are obtained and stored in a central repository accessible by the DCL Coordinator. Consideration should be given to adapting the Housing Agreements to include all relevant information for the waivers. This should be completed by May 31st, 2017.

F.5.2 The General Manager, Community Services should ensure that the DCL coordinator is notified in advance by the Housing Planner of any projects requesting DCL waivers and that the project meets all waiver criteria. This should be completed by May 31st, 2017.

Management Response:

Please check one:

☒ Agree with the findings

☐ Disagree with the findings

Please check one:

☒ Agree with the recommendation

☐ Disagree with the recommendation

Other issues for management consideration:

F.6 Improve reporting capabilities in POSSE system for DCL waivers

DCL information in CSG DCL tracking system

A standalone database referred to as the 'CSG DCL tracking system' is used to track all Development Cost Levies. Upon collection of the DCL and waiver amount, the DCL Coordinator manually enters the DCL transaction information into the CSG DCL tracking system for record keeping purposes. The database is used by Financial Services and Planning for annual reporting on DCL waivers.

The CSG DCL tracking system is a separate database that is not linked to the permit issuance process and relies on manual data entry. Along with the risks inherent to a standalone system there is potential for errors to be made which may impact annual reporting of DCL waivers.

DCL information in POSSE system

POSSE is the new permit licensing system implemented in 2016 which replaces older permitting systems such as Amanda and PRISM. DCL information is entered into POSSE by the DCL coordinator during the permit issuance process. As POSSE is the City's central permit licensing system for all building developments going forward, it should be relied on as the key source of information for DCL waivers. There is some duplication of work in manually entering some of the same data in two separate systems. However, based on discussion with management, there is currently limited reporting capability in POSSE to facilitate the annual reporting of DCL waivers.

Recommendation:

F.6.1 The General Manager, Development, Building & Licensing should work with IT to investigate the possibility of developing reporting capabilities in POSSE on DCL waivers issued. It should also be investigated whether it is practical to eliminate the standalone system. This should be completed by July 31st, 2017.

Management Response:

Please check one:

☒ Agree with the findings

☐ Disagree with the findings

Please check one:

☒ Agree with the recommendation

☐ Disagree with the recommendation

Management Comment:

F.6.1 - DBL will work with CoV IT to determine whether there is a mechanism in POSSE, a package software application, to better track and report on projects that have been granted waivers. The timing of implementation will depend on the complexity of the updates and the workload capacity of the IT Team.

Appendix A

Results of review of 30 DCL waiver projects

#	Address	Does not meet Rental 100 requirement for 100% rental	Waiver calculation discrepancy
1	1142 GRANVILLE ST		
2	1718 DAVIE ST		
3	1850 VICTORIA DIVERSION		X
4	1061 BROUGHTON ST		
5	2778 E HASTINGS ST		
6	1549 W 70TH AV		
7	8555 GRANVILLE ST		
8	1650 QUEBEC ST		
9	5711 RHODES ST		
10	8198 CAMBIE ST		
11	2525 CARNARVON ST		
12	1388 CONTINENTAL ST		
13	2215 E HASTINGS ST		
14	191 E 11TH AV		
15	245 E GEORGIA ST		
16	1568 E KING EDWARD AV		
17	1398 RICHARDS ST ¹	X	
18	333 E 11TH AV		
19	1408 E 15TH AV		
20	1408 E 41ST AV		
21	1910 FERNDAL ST		
22	609 HEATLEY AV		
23	968 KINGSWAY		
24	388 SKEENA ST		
25	4320 SLOCAN ST		
26	308 W HASTINGS ST		
27	288 E HASTINGS ST		
28	303 E PENDER ST (450 Gore St)		
29	179 MAIN ST		
30	3699 MARINE WAY		
Total		1	1

¹ 1398 Richards Street is the address of the Charleson project.

Appendix B

DARCI Grid: DCL Waiver Process

<u>PHASE</u>	<u>DECIDER</u> <i>Holds the ultimate power over the process</i>	<u>ACCOUNTABLE</u> <i>Person fully accountable for the process</i>	<u>RESPONSIBLE</u> <i>Those responsible for doing the work</i>	<u>CONSULTED</u> <i>Those from whom input is solicited</i>	<u>INFORMED</u> <i>Those to be kept apprised of information</i>
<u>Overall Process:</u>	- GM, Planning, Urban Design & Sustainability	- GM, Planning, Urban Design & Sustainability	- Planner, Housing Policy and Projects - Lawyer	- DCL Coordinator - Director, Real Estate Services - Project Coordinator, Development, Buildings & Licensing	- Developer
1. Approval of Rental 100 project	- GM, Community Services	- GM, Community Services	- Planner, Housing Policy and Projects - Project Coordinator, Development, Buildings & Licensing	- Director, Legal Services - GM, Planning, Urban Design & Sustainability - GM, Development, Buildings & Licensing	- Developer
2. Finalize Housing Agreement	- GM, Community Services	- GM, Community Services - Director, Legal Services	- Lawyer - Planner, Housing Policy and Projects	- Developer - Developer's legal team	- Developer
3. DCL calculation	- GM, Development, Buildings & Licensing	- GM, Development, Buildings & Licensing	- DCL Coordinator - Manager, By-law Compliance	- Planner, Housing Policy and Projects - Project Coordinator, Development, Buildings & Licensing - GM, Planning, Urban Design & Sustainability	- Developer
4. Approval of DCL waiver	- GM, Community Services	- GM, Community Services	- Planner, Housing Policy and Projects - Lawyer	- DCL Coordinator - Director, Real Estate Services - Project Coordinator, Development, Buildings & Licensing	- Developer

Appendix C

Recommended Changes to DCL Waiver Process

- Establish governance and accountability (F.1.1)
- Establish business process for management review of DCL calculations (F.2.2)
- Review and correct waiver discrepancy noted (F.2.3)
- Verify rental rate criteria at waiver application and initial occupancy (F.4.1)
- Investigate reporting capabilities in POSSE system (F.6.1)

