Evaluation of Previously Presented MDC Models

This attachment provides an overview of the MDC "Superlight," MDC "Light" and MDC "Heavy," the MDC models evaluated and presented at a Special Executive Committee meeting on November 26, 2015 in report CR_2132. A high level description of the three types of MDCs as well as the current In-House model are provided below. For additional information related to the models, please refer to CR_2132.

In this attachment:
- Table 1 provides an overall relative rating of each MDC model relative to the current In-House model.
- Table 2 outlines the overall financial impact (costs and revenue) of each of the three MDC models based on the financial analysis completed in 2015 for report CR_2132.

Description of Previously Presented MDC Models

There are some common elements between all three evaluated models, including:
- All are for-profit MDCs.
- A small batch of high-opportunity properties would be initially transferred to the MDC at fair market value, but payment for the land would not occur until the MDC was profitable. The exact number and type of properties changes depending on the model (range was from four to six properties).
- The City would need to subsidize initial startup and operating costs until the MDC was self-sufficient.
- Cash grants would be provided to MDCs and would not be repaid. The amount of the grant increases from MDC Superlight to MDC Light to MDC Heavy.
- Dividends would not be paid to the City until the MDC was self-sufficient.
- All of the MDC models presented would not replace the existing in-house model or reduce the capacity of the in-house model.

<u>MDC Superlight</u>
This was the model recommended in CR_2132.
- First three to four years of operation were anticipated to cost a total of $22.65 million to the City with no dividend payment over the same time period (refer to Table 2, below).
- Projected Internal Rate of Return = six to nine per cent.

- Performs a very narrow set of activities.
    - Primary activities involve land value-enhancement activities (plan amendments, rezoning, etc.)
    - No servicing or development costs are assumed.
    - Some participation in onsite development through land equity contribution.
- Enter into projects with private developers for onsite development.
- Primary revenue stream would be through sale of value-enhanced lots and some onsite development equity share.
- Small board of directors (five).
- Team is comprised of chief executive officer with a small staff complement (up to three staff).

<u>MDC Light</u>

Land value is enhanced but no servicing or development costs are incurred; enter into projects with developers.

- First three to four years of operation were anticipated to cost a total of $32.40 million to the City with no dividend payment over the same time period (refer to Table 2, below)
- Projected Internal Rate of Return = 3.1 per cent.
- Performs a very narrow set of activities.
    - Primary activities involve land value-enhancement activities (plan amendments, rezoning, etc) as well as site servicing.
    - Some participation in onsite development through land equity contribution.
- Enter into projects with private developers for onsite development.
- Primary revenue stream would be through sale of serviced lots and some onsite development equity share.
- The number of people sitting on the Board of Directors was not stated, but would likely be similar to MDC Superlight.
- Team composition was never stated, but would likely be similar to MDC Superlight with some additional staff with experience in site servicing activities (CEO and up to five staff).

<u>MDC Heavy</u>

Land is fully developed into residential, commercial or industrial properties through projects with developers; properties are leased/rented to tenants.

- First three to four years of operation were anticipated to cost a total of $218.57 million to the City with no dividend payment over the same time period (refer to Table 2, below).

- Projected Internal Rate of Return = 2.0 per cent.
- Performs full range of land development activities including:
    - Land value-enhancement activities (plan amendments, rezoning, etc)
    - Site servicing or development.
    - Onsite development including vertical development.
- Enter into projects with private developers for onsite development.
- Revenue stream would be through sale of vertically developed properties or ongoing lease/rentals of developed properties.
- The number of people sitting on the Board of Directors was not stated, but would likely be larger than that of the MDC Superlight.
- Team composition was never stated, but would likely be substantially larger than the MDC Superlight to ensure there was in-house experience related to the full range of land development activities.

<u>Current In-House Model</u>

- The evaluation below only takes into account the City's current approach to the delivery of surplus lands and does not include delivery of other lines of work, such as greenfield and transformational projects, as the MDCs were never intended to deliver those projects.
- Activities are similar to the MDC light and include:
    - Land value-enhancement activities (plan amendments, rezoning, etc)
    - Site servicing.
- The City is not currently involved in onsite or vertical land development activities. Properties are sold to private developers to allow them to develop lands in a similar fashion to the Calgary Municipal Land Corporation.
- The City currently does not typically seek development opportunities with the private sector

Evaluation

The following Table 1 provides an overall performance comparison to various factors relative to the current, in-house delivery model. The models evaluated are noted above and were only considered to deliver on four to six select, high-opportunity properties. Ratings of Much Worse, Worse, Equivalent, Better and Much Better were applied to the various factors. Explanations for scoring are provided for each factor category below Table 1.

Table 1 - Relative Rating of each MDC Model compared to current In-House model

Factor	MDC Superlight	MDC Light	MDC Heavy
Start-up			
Time to Set-up	Worse	Worse	Much Worse
Cost to Set-up	Worse	Worse	Much Worse
Operations			
Nimbleness	Better	Better	Better
Flexibility to Work with Third Parties	Much Better	Much Better	Much Better
Leverage private sector financing	Much Better	Much Better	Much Better
Ability to leverage City resources	Much Worse	Much Worse	Much Worse
Governance			
Ability to Accept Council Input	Much Worse	Much Worse	Much Worse
MDC Mandate or Project Continuity After Election	Much Better	Much Better	Much Better
Perceived conflict of interest with City	Better	Better	Better
Municipal Alignment			
Ability to re-align to changing City objectives	Much Worse	Much Worse	Much Worse
Support City projects	Much Worse	Much Worse	Much Worse
Financial			
Ability to borrow for development activities	Better	Better	Much Better
Impact to City Debt	Worse	Worse	Much Worse
Revenue Generating[1]	Equivalent	Worse	Worse

[1] Based on financial analysis completed in 2015's CR_2132

Self Sustainable[1]	Worse	Much Worse	Much Worse
City access to Revenue	Worse	Worse	Worse
Requirement to pay property tax	Much Worse	Much Worse	Much Worse
Requirement to pay income tax	Equivalent	Equivalent	Equivalent
Legal & Risk			
Risk Exposure to the City	Much Better	Much Better	Better
Subject to FOIP	Equivalent	Equivalent	Equivalent
Subject to public procurement in alignment with NWTPA	Equivalent	Equivalent	Equivalent
Project Delivery			
Deliver Surplus Lands	Equivalent	Equivalent	Equivalent
Undertake onsite and vertical development	Better	Better	Much Better
Creating new lines of business	Better	Better	Better

Start-up

Creating an MDC requires both time and money. The amount of both increase with the complexity of the MDC and the diversity in the amount of land development activities it is involved in, which is reflected in the evaluation. Table 2, below, outlines the costs associated with the startup of each MDC.

Operations

As a separate entity from the City, an MDC would not necessarily be subject to all City policies and procedures. This would result in increased nimbleness and, partially, an improved ability to work with the private sector, granting access to private sector financing. While the City has entered into contractual agreements with the private sector for land development purposes in the past, it needs to be considered on a case-by-case basis. In general, it is anticipated that an MDC would be able to enter into agreements with the private sector more easily than the City could.

This separation does have the negative impact of eliminating or greatly reducing the MDC's access to City resources such as legal, financial and risk services, or the combined knowledge of the many business areas throughout the City.

Governance

The separation from the City ultimately reduces the amount of input Council has on an MDC, which reduces the MDC's ability to act as a tool to achieve Council's vision as it shifts over time. Council also has a reduced ability to course-correct if it feels the MDCs objectives no longer align with Council's vision. However, the political separation does grant the MDC improved stability over time as Council's change along with their respective priorities.

During the previous engagement work with the private sector that was carried out in 2015's CR_2132, there was some concern expressed over a perceived conflict of interest with the City acting as both developer and regulator. While an MDC would provide greater separation, it was still noted as a potential issue.

Municipal Alignment

The separation from the City does reduce its overall ability to align with the Municipality. Given that the mandate is set at the creation of the MDC and, generally speaking, does not change, there may be a reduced ability for the MDC to maintain alignment with changing City objectives.

The separation also reduces the MDC's ability to incorporate City-building projects and objectives into its land development activities.

Financial

The previous analysis found that the financial impacts of establishing an MDC can vary significantly given the types of MDCs and their different activities. MDCs are able to borrow for land development. Of the three MDC models evaluated, only the MDC Heavy was intended to borrow significant amounts. However, this debt, along with any revenues, are included in the City's debt limit calculations. In the short-term, this would likely have a negative impact on the City's debt calculations, but over time, if an MDC was profitable, it may have a positive impact. However, this long-term projection was not completed beyond the initial group of properties.

The MDC models presented in 2015's CR_2132 were not found to have a substantial internal rate of return. Internal rate of return is calculated using initial cash investments, annual cash flows, and time to determine if an investment will generate enough annual growth to justify the cost. Of the three models evaluated, only the MDC Superlight was able to generate a high enough internal rate of return to justify further consideration. This inability to generate sufficient revenue relative to cost would negatively impact the MDC's ability to be self-sustaining.

Separation from the MDC would eliminate the City's access to the MDC's cash reserves. While revenue generated from land development activities is not intended to be used to finance non-related work, it is occasionally used as an interim funding source. For example, Land Enterprise Retained Earnings is being used as an interim funding source for 55 per cent of the coliseum demolition costs.

The City is not required to pay property tax or income tax as part of its land development operations. However, an MDC would be subject to property tax. An MDC that is at least 90 per cent owned by the municipality would not be subject to income tax. All of the models reviewed were anticipated to be solely owned by the City and therefore would not have to pay income tax.

<u>Legal and Risk Exposure</u>
One of the greatest advantages of an MDC is the improved risk protection provided to the City. This is due to the MDC being a separate legal entity from the City that is accountable for its own operations. Due to the City having limited control over an MDC's operations, it has limited liability as a result of those operations. Given the MDC Heavy's more risky land development work, there would be a larger risk associated with it.

Due to the MDC still being a City-controlled entity, it is subject to the *Freedom of Information and Protection of Privacy Act* (FOIP), as well as requirements of the Northwest Partnership Trade Agreement (NWTPA). Under NWPTA, an MDC would still be required to publicly procure development partners, consultants and contractors.

<u>Development Projects</u>
The previous MDC evaluation in 2015's CR_2132 only considered the MDC performance based on four to six select surplus properties. In terms of the ability to dispose of the surplus lands, there would be a relatively equal performance to the City's current in-house model.

These MDCs were also intended to carry out onsite and vertical development work, something which the City does not do currently. The MDC Heavy was able to undertake these activities on its own or through partnerships, whereas the other models were only able to do so through partnerships.

Financial Impacts

Table 2 - Total Financial Impacts to the City in the Short-Term (3-4 years) by Creating an MDC (as presented in 2015's CR_2132)

Count & Score	MDC Superlight	MDC Light	MDC Heavy
Number of Properties Initially Transferred	5	6	4
Land value transferred to MDC	$ (17.90)	$ (27.50)	$ (26.05)
Cash grants provided by City to MDC (Start-up costs and initial operating costs)	$ (3.75)	$ (4.90)	$ (15.88)
Paid in Capital	$ -	$ -	$ (48.50)
Guaranteed Loans	$ (1.00)	$ -	$ (128.14)
Dividend payment to City from MDC	$ -	$ -	$ -
Total Financial Impact to City	**$ (22.65)**	**$ (32.40)**	**$ (218.57)**
- All amounts in millions. - All amounts are from 2015 and have not been adjusted for 2023			