

**July 31, 2015**

## **Proposed Edmonton MDC--Real Estate Experts Report**

### **Preamble:**

This is the final summary report of the team of Real Estate Experts who have been retained by the Sustainable Development Department of the City of Edmonton to provide input and strategic support to the process of examining the potential of the City of Edmonton establishing a Municipal Development Corporation (MDC).

We are making a series of recommendations that include a number of high level principles that, if Council decides to proceed with the establishment of an MDC, should be included in its operating philosophy and may form a part of the Shareholder Direction that would be provided to the new Board of Directors from City Council. In addition, we identified the need to improve the process the City uses to identify and declare various lands that are surplus or underutilized so that more prominent and high value sites can be redeveloped. The establishment of an Edmonton MDC is a very significant initiative and one that, if implemented effectively, can provide potential for both financial and City-Building benefits to the City of Edmonton over a long period of time. Similarly, if this project is not conceived and implemented effectively then the City of Edmonton will be exposed to significant risk, both on a long term financial basis and in eroding the confidence of the real estate and development community in Edmonton.

### **Summary Recommendations:**

#### **The Real Estate Experts Team Recommends to the City of Edmonton:**

1. That if the City of Edmonton decides to implement a Municipal Development Corporation (MDC), then the high level principles outlined in section 3.1 of our report be included in the foundation documents for the new corporation;
2. That the City of Edmonton establish an ongoing engagement process with the Real Estate and Development Community in Edmonton to improve communication and collaboration, identify emerging issues and resolve potential conflicts in a model that is mutually supportive and transparent;
3. That if the City of Edmonton decides to implement an Edmonton MDC, then Council consider the transfer of other major City of Edmonton development projects to the MDC for ongoing advice, oversight and implementation;
4. That the City of Edmonton continue to identify high value, complex and municipally significant sites that would be appropriate to turn over to the MDC for development;

5. That if the City of Edmonton does not implement an MDC, then in order to improve the overall functioning of the Real Estate function, then the City Establish an “Internal Pilot” similar to an MDC Model that would focus on internal improvements to the land function in order to improve ongoing functioning with the private sector and to maximize the value creation opportunity on these surplus sites;
6. That the governance model for a potential MDC continue to be refined using best practices in both public and private sector corporate governance to provide the MDC with leading edge development expertise, particularly during the start-up phase and beyond.

## **1.0 Background:**

### **1.1 Our Team:**

Our team of Real Estate Experts were retained by the City of Edmonton as part of a competitive RFP process on May 4, 2015. The group consists of a consortium team of four organizations that represent best in class real estate expertise, development experiences, local Edmonton Market knowledge, and extensive knowledge of Municipal Development Corporations in North America. They include:

#### **John A. Macintyre, Principal, Cresa Toronto Inc.**

The team is led by John A. Macintyre, Principal with Cresa Toronto Inc. Cresa is an international Real Estate strategy, consulting and brokerage firm with offices in four Canadian cities and over 60 international offices. John leads the Strategic Real Estate and Public Sector Practice Groups in the Toronto office and is the lead Principal on all Development projects. He is a former long-term senior Municipal Official as Director of Parks, Forestry and Recreation in the City of Toronto, and spent five years as Senior Vice-President of Build Toronto where he led the start-up process as the lead on all corporate services and shareholder relations and led the residential land development group where he was responsible for a range of large development projects. John is very active on a number of Boards and holds the professional designations as a Chartered Director and Human Resources and Compensation Committee Certification from the Directors College.

#### **J. Lorne Braithwaite, President Park Avenue Holdings Inc.**

Park Avenue Holdings is a Real Estate Advisory and Development company owned by Principal J. Lorne Braithwaite. Park Avenue Holdings is active in the real estate development sector in a number of asset classes and provides advisory services to a number of private sector clients.

Lorne became CEO of Build Toronto in early 2009 following a lengthy career in real estate, where he was previously CEO of Ivanhoe Cambridge, the Development Arm of the Caisse de Depot (the Quebec Pension Plan). Lorne has developed major projects in all major Canadian cities, including Edmonton and other locations in Alberta. Lorne is also a highly respected Corporate Director, having served on the Board of Directors of Calgary-based Enbridge Inc., a former Director of Bata Shoe Corporation and is currently the Chair of the Investment Committee at the Canada Post Pension Plan. A long-time resident of Alberta, Lorne has strong connections in Edmonton and is an alumni of the University of Alberta, where he is a member of the Business Advisory Council for the School of Business in Edmonton.

### **John Day, John Day Developments**

Prior to devoting his full attention to real estate development, John Day was a partner and senior practice leader at Fraser Milner Casgrain LLP (FMC), now Dentons LLP. At FMC, John Day specialized in real estate law and commercial transactions. John Day is an alumnus of the University of Alberta and he was appointed Queen's Counsel in 1990. A long term member of the Law Society of Alberta (now inactive), he has been involved in a number of different community organizations. He is currently involved in the community in the following capacities: McEwan University, Chairman of the Board of Governors; Royal Alexandra Hospital Foundation, Past Chairman of the Board. Mr. Day is also currently involved in private businesses including Marmot Basin, Chairman of the Board; Mountain Park Lodges, President; Jasper Tramway, Chairman of the Board, and principal of John Day Developments Ltd.

A prominent businessman and renowned developer, John Day has built a substantial real estate portfolio through his ability to identify key assets in strategic locations.

### **Kevin McKee, Pangman Development Corp.**

Kevin McKee founded Pangman in early 2010 and has extensive experience in all aspects of the commercial real estate industry. After graduating from the University of Alberta (B. Comm, Finance), he began his career with Avison Young, rising to become Managing Partner in 2001. From 2003 to 2010, he was Vice President of Investment at WAM Development Group. He formed Pangman Development Corporation, a project management and real estate holding company in 2010. Pangman focuses on providing development management services to select private investors, as well as growing a portfolio of revenue-producing assets through acquisition and greenfield development. The company's development management services include land acquisition, rezoning, pre-development, design, permitting, construction, marketing, leasing, and sale or refinancing at project completion. Kevin is heavily involved in the Edmonton Community and plays a leadership role to many initiatives.

This team provides the ideal mix of strong local knowledge, impeccable professional reputation, incredibly diverse real estate and development background and leading-edge experience working in Municipal Development Corporations.

## 1.2 Our Terms of Reference:

The key elements of our assignment are to:

1. Support the administration in evaluating the potential for establishing a Municipal Development Corporation in the City of Edmonton;
2. Provide input and expertise to evaluate individual development sites;
3. Engage the stakeholder community from the real estate and development sector in Edmonton to gauge their interest and assess the potential for acceptance of an MDC;
4. Support Deloitte in the development and evaluation of a financial model, a strategic and operational plan; and,
5. Provide input and strategic advice on different operating models, governance structures and overall strategy for establishing a MDC.

We have been involved in virtually every aspect of the workplan to evaluate the City's potential involvement in a MDC, have attended all of the start-up team and stakeholder meetings and have provided a significant range of input to this assignment.

## **2.0 The Major Work Areas:**

### 2.1 Identification, Review and Analysis of Properties:

Our team visited each site identified by the City of Edmonton as potentially available for transfer to the MDC, and we developed high level strategies on what we considered to be highest and best use on each site, and developed initial financial proforma for development at each of those sites. Working with Deloitte, we rolled up all of this information to develop a five year projection of revenues and expenses associated with development on each site and for the MDC as a whole.

### 2.2 Stakeholder Consultation:

Our Real Estate team developed a strategy for enhanced communications and liaison with the broader development and real estate community in Edmonton; this group has been vocal in their opposition to the perception that the City is getting into the development business to compete with the private sector. Our engagement framework was done in two stages, an initial engagement process consisting of informal individual and small group discussions and two more formal consultation sessions with the real estate and development community on June 22 and July 13, 2015. While the formal outcomes of the stakeholder consultation are documented in the staff report, we will

make some comments and observations on the prevailing attitudes of the development community in our recommendations.

### 2.3 Operating Models:

In conjunction with Deloitte, our team has developed a continuum of different models which is outlined in the main body of the report. “MDC Heavy” refers to the model that would have a larger more robust organization and Board of Directors and would be a “full service” developer including investing equity capital into deals and working through the entire development cycle.

The “MDC Lite” model would use a similar organizational structure as “MDC Heavy”, but would be involved in the front end of the development process and would make investments into transactions consisting of only equity land contributions.

The “MDC Superlight” is a scaled down model with a smaller organization and smaller Board of Directors and would be involved in a similar model as the “MDC Lite”. While it would have more limited capacity, the MDC has advantages in that it is scalable and would be able to ramp up over time as the balance sheet is established and projects are completed.

We do not believe that there is any merit in proceeding with the “MDC-Heavy” model identified within the continuum of options in the report. The “MDC Heavy” option would require significant capital and underwriting of debt, will require more property than has currently been identified and in particular, higher quality sites to be included. MDC Heavy is not predicted to make a sufficient return on the investments required to make it successful, exposing the MDC and the City to substantial risk. It is not supportable or prudent to proceed with this model at this time.

The “MDC Lite” model, while having a positive financial return, does not meet the investment return objectives and is not recommended.

We will provide qualified support for the implementation of the “MDC Superlight” model, where all properties are developed in conjunction with the private sector and where the City and the MDC will participate in joint ventures that do not require additional equity participation, thus limiting the risk to the “value added” land value that is put into individual projects. Our qualified support reflects the merits of the overall objective of establishing an MDC model, will provide the City of Edmonton with a “Real Estate Center of Excellence” which will improve the overall functioning of the Real Estate and Development model for the City and enable it to leverage the development expertise of the MDC Board and Staff for better outcomes for Edmonton. This version of an

organization would be leaner and would be scalable in the future as the balance sheet is established and their deal credibility in the marketplace improves.

One critical element is that financial returns are in part governed by the appraisal system of lands going into the MDC and it is essential that lands being conveyed to the MDC from the City of Edmonton are transferred on an appraised market value basis when moving into the title of the MDC.

#### 2.4 Governance:

Our team reviewed the key Governance models and risks associated with each and provided input to Deloitte on the key issues related to governance. We worked with the City of Edmonton Legal staff to examine the key risks and opportunities on different models, including for-profit and not for profit models and discussed a range of mechanisms to provide broad shareholder direction to a new MDC Board of Directors without incurring additional liability for the City. Our findings are outlined in the governance section.

#### 2.5 Strategy:

Our team reviewed development strategy, in general terms and across the different asset classes, both from the Private Sector standpoint and from an MDC standpoint. We evaluated risks associated with each element and provided input to City Officials and Deloitte which was incorporated into the financial modelling.

#### 2.6 Financing:

Our team examined different financing requirements and strategies and provided an assessment of impact of different financing models with respect to debt load and underwriting of City debt guarantee. Both equity and debt capital needs will be provided by private and public sources with the land being MDC's contribution

#### 2.7 Key Principles:

Our team developed and tested a range of key principles that the City should consider if it decides to proceed with establishing an MDC in Edmonton. These are outlined in a separate section in the body of this report.

#### 2.8 Internal Processes:

Our team did a cursory evaluation of internal processes for the identification and surplus designation of City lands, and we have identified a body of future work which will be required, regardless of if MDC proceeds to streamline internal processes.

### 3.0 Findings and Recommendations:

This section of the report deals with our major findings and recommendations. Each of the recommendations from this section are highlighted with some comments and additional discussion.

#### ***3.1 If the City of Edmonton decides to implement a Municipal Development Corporation (MDC), then the high level principles outlined in this section of our report be included in the foundation documents for the new corporation.***

##### Comments:

Through our consultation process and based on the extensive work that we have undertaken on this project, if the City of Edmonton is going to proceed with the implementation of a MDC, then we have a number of key principles that should provide overall strategic guidance to the establishment of the corporation.

These include:

- ***All sites will be developed through partnerships with the Private Sector,*** which includes selling “value enhanced” land through an RFP process or developed in partnership with the Private Sector. The MDC should not develop a large internal structure to deliver projects which will require major commitment to overhead and should focus on using the capability of the very robust private sector development expertise in Edmonton. The MDC should focus on front-end conceptualization of projects and initial planning and value creation activities, but the actual delivery should be done in conjunction with Private Sector Partners.
- ***The MDC will not purchase land except where it is adjacent or required to enhance an existing MDC or City Owned Property.*** One of the issues that we heard loud and clear at the Stakeholder consultation process was the fear from the private sector that the MDC would compete in the open market for non-city owned lands, and they would have a significant competitive advantage over the private sector. Our team believes that the MDC should not engage in additional property purchases except where it is adjacent or connected to existing MDC or City of Edmonton owned sites, or is required to complete a property consolidation related to an MDC site. We believe that this will be more palatable to the Private Sector community and addresses their immediate concerns. After the MDC has been established and has an operating history and a stronger working relationship with the Private Sector, then this principle could be revisited. The Private Sector MDC Board could examine sites that have been vacant for substantial amount of time with the objective of activating the site, but the MDC should not generally be acquiring vacant lands on the open market.



- ***The MDC will have an open and transparent RFP process to select partners.*** Our team believes that the MDC should have a clear and accountable RFP Process in order to select private sector partners. The RFP Process should be developed and approved by the Board of Directors with the input of the private sector. This is a clear “best practice” in governance and should be included in the shareholder declaration.
- ***The MDC will use best practices in partnership development including shared risk/reward and equity contributions to be a “real” contributing partner.*** Similar to the previous point, the MDC should use best practices in partnership development which should be embedded in its shareholder declaration.
- ***The MDC will publish performance metrics and financial statements as part of an annual report process to the City of Edmonton;*** this principle is self-explanatory.
- ***The MDC will be supported by a board of directors with real local, regional and national development and real estate investment experience with a strong corporate governance culture;*** This is one of the most important elements of establishing a MDC and a diligent and robust process should be used to recruit, select and orient the new MDC board. It should be set up to provide strong leadership with industry-best experience in Real Estate development and have a full set of the critical skills amongst the directors to ensure that the start-up of the new corporation is successful. The makeup of the Board should be a full private sector approach with no direct City of Edmonton Council membership be established to minimize political risk and ensure that the organization functions as an effective arms-length company. This board recruitment process should be the subject of a further analysis.
- ***The MDC cannot function as “another department of the City of Edmonton” or it is likely to fail.*** This concept is important to recognize as it will be tempting for the Civic administration to ask the MDC to undertake projects that will have a significant opportunity cost in terms of time and focus that would not be spent on other higher value projects. The MDC must be a hybrid between the public and private sectors, and will need to be closer aligned to the private sector in terms of its operating practices.



***3.2 That the City of Edmonton establish an ongoing engagement process with the Real Estate and Development Community in Edmonton to improve communication and collaboration, identify emerging issues and resolve potential conflicts in a model that is mutually supportive and transparent.***

Comments:

Our team led a major outreach and consultation strategy with the broader real estate and development community in Edmonton. This included a broad range of industry organizations such as UDI, NAIOP, BOMA, CHBA and the Edmonton Chamber of Commerce. We also had several sessions with focus groups and larger, more formal consultations with individual developers, home builders, industrial developers and the brokerage community. Edmonton is indeed fortunate to have a very robust and successful development community and our assessment is that they genuinely care about the City and want the City to be successful and prosperous. However, we also noticed an underlying theme of mistrust and a general lack of engagement and communication between the City Administration and the broader development community. Outside of this process and whether or not the City of Edmonton proceeds with establishing an MDC, the City should consider a more formal engagement mechanism that can be put in place to improve communications, two way engagement and tap into the significant talent that the Development community possesses. A formal set of terms of reference should be established and there are a number of models that could be considered, but the message that it would send to this important community would be significant.

***3.3 That if the City of Edmonton decides to implement an Edmonton MDC, then Council consider the transfer of other major City of Edmonton development projects to the MDC for ongoing advice, oversight and implementation.***

Comments:

One of the key benefits of establishing a MDC is that it will significantly bolster the capacity of the broader City of Edmonton “family” in dealing with real estate and development issues. The MDC should be viewed as a “center of excellence” in real estate and development practice and in addition to the general sites that have been identified, the City of Edmonton has some very major development sites which are large and complex and the City would benefit from an oversight process that includes the expertise and knowledge of the MDC Board of Directors and Staff. While we recognize that transferring the entire roster of complex projects, some of which require substantial capital infusion from the City, is not practical, nonetheless, some way to tap the experience of the MDC should be considered, especially with a

view to improving the overall level of real estate expertise and improving the relationship with the Private Sector.

***3.4 That the City of Edmonton continue to identify high value, complex and municipally significant sites that would be appropriate to turn over to the MDC for development;***

Comments:

The process that the internal Administration of the City has undergone to identify suitable properties that could be transferred to the MDC has been completed in anticipation of this MDC process. However, it is clear that this process, while at the formative stages, does have the opportunity to be further optimized to identify other potential vacant, surplus or underutilized sites must be reviewed for emerging opportunities. In particular, the Real Estate Expert team has identified the general lack of large, complex and potentially more valuable City-owned sites, particularly in the downtown core, where there will be a more significant development opportunity and where there are more robust City building outcomes. This could include sites that currently contain Civic Infrastructure such as office buildings, libraries and recreation facilities, and other complex sites where a multitude of interests could align such as sites that are located at Transit nodes, or where current City uses might not use the facility to its greatest potential. We believe that a further review of the process and some additional refinement with the support of Senior Officials would be of benefit.

As part of this point, we should also indicate that the value add of a MDC is the fact that it can tackle projects that private sector developers are hesitant to take on so it should focus on its key attributes and its ability to bring multiple partners together where there are environmental challenges, difficult land assemblies or complex infrastructure environments. The MDC should stay away from simple projects where they can add little value such as more straight forward industrial sites, the exception to this principle being that where a simple site might be monetized in order to make the investment in another project be realized.

***3.5 That if the City of Edmonton does not implement an MDC, then in order to improve the overall functioning of the Real Estate function, then the City Establish an “Internal Pilot” similar to an MDC Model that would focus on internal improvements to the land function in order to improve ongoing functioning with the private sector and to maximize the value creation opportunity on these surplus sites;***

#### Comments:

If the City decides not to proceed with establishing an MDC, then there are some other enhancements to the current system of managing the Real Estate function which we have labeled as “MDC Internal Pilot”. This pilot would consist of a small internal team with enhanced real estate development expertise embedded within the organization and reporting at a senior level. The objectives of this ground would be to improve relationships with the Private sector development community, enhancing the value of land prior to it being sold to the development community and assisting in identifying internal City property and infrastructure assets that could be redeveloped to enhance the dual outcomes of better financial returns and city building outcomes. In order to increase throughput and potentially capture additional value on some surplus sites they would also require some adjustments to some internal processes including potential changes to the delegated authority limits to allow a faster turn-around and a streamlined process. If this MDC “Internal Pilot” were implemented, it would allow a faster transition to a full MDC model in the future if Council were to decide to implement an MDC in the future.

### ***3.6 That the governance model for a potential MDC continue to be refined using best practices in both private and public sector corporate governance and in order to provide the MDC with leading edge development expertise particularly during the start-up phase.***

#### Comments:

Our team has significant corporate governance experience in both public, private and not-for-profit organizations and we suggest that the establishment of the Board of Directors of the new MDC organization is likely the most critical factor of success in the start-up period. Not only must the proper governance structure be put in place, but the makeup of the board in terms of the complex skills matrix that is required and the legislative and policy framework that the board is able to operate within, is equally important. In particular, the structure must eliminate or at least control the element of political risk so that the MDC can operate independently from City Council and the Civic Administration and this is why we are advocating for a fully private sector Board with no direct membership from the City of Edmonton. While there are some unique challenges that arise from the requirement to obtain Provincial Approval to establish the MDC, and the need to show a profitable return by the third year of operation, a strong, well-functioning board will mitigate a number of these challenges.

We have also investigated the notion of potentially establishing the MDC as a non-profit corporation. On the surface, there may be some merit in a non-profit model as it would not require Provincial approval to establish and could do virtually all the activities that a for-profit corporation could with the exception of being able to

declare cash dividends to the City. It would be limited to providing City Building benefits to the City of Edmonton which could be an alternative to cash dividends if these were taken in the form of contributions to affordable housing, civic infrastructure renewal, to transit infrastructure or public realm improvements. While the private sector stakeholders would likely have more support for a non-profit model, the main complication with this model is that it would be much more complex to wind up in terms of potentially stranding assets within the MDC or one of the subsidiary corporations that would be set up to hold joint venture partnerships. On balance, Council will have to determine if the non-profit or for-profit models would be preferable if they elect to proceed with the MDC. However, financing these projects may prove to be challenging if it was done under a non-profit model.

We should also note that one challenge to be addressed in establishing a new organization is going to be attracting the right executive talent with the right combination of development experience and overall corporate leadership capability and being able to accomplish this within the operational and financial conditions that will be established. This is a task that will fall to the MDC Board once it is established but should be noted as one of the implementation challenges.

#### **4.0 Summary**

This project has been very challenging and we have sought to balance the range of information and inputs to this process with our team's extensive knowledge of both the development process and the unique challenges of the operations and politics of municipal development corporations.

While the financial metrics do not support the implementation of the "MDC Heavy" model due to extensive capital and debt requirements coupled with a higher risk profile and lower than acceptable returns, there is some merit in proceeding with the less risky "MDC Superlight" model. This would allow many of the benefits of an MDC without the capital and debt requirements, while the primary benefit would be the establishment of a "Centre of Excellence" in Real Estate Development which would enhance the ability of the broader City of Edmonton family to understand, strategize and collaborate with the extensive private sector network of real estate and development organizations in the Edmonton Community.

If Council approves the MDC, it will be critical to continue the exercise of identifying and freeing up additional high-potential sites so that the MDC will have some high profile and more complex sites that will enable it to show its value in the short to medium term. Council should also consider what role the experts at the Board and Executive Staff level of the MDC could play in several long term and high value sites requiring a high level of expertise in other major City of Edmonton Real Estate Development projects.

We have outlined a series of high level principles that we believe are critical to a successful launch of the MDC and should be enshrined in the governance model and directions to the new Board of Directors of the MDC.

Finally, the City of Edmonton is indeed fortunate to have a robust, capable and highly engaged private sector network of real estate and development professionals. The City and the MDC must strengthen the relationship with this important sector; we believe that the establishment of an MDC is but one element of advancing that relationship, which also requires an ongoing collaborative structure. It is clear from the input of the private sector that this is one of Edmonton's most skilled and successful industries, and to access their skills and expertise presents a unique city-building objective unto itself.

We look forward to the balance of this project, including the deliberations of Edmonton City Council.

Respectfully submitted,

Real Estate Experts Team

Cresa Toronto Inc., Park Avenue Holdings, John Day Developments, Pangman Development Corporation.