



The Corporation of **THE CITY OF NORTH VANCOUVER**  
**FINANCE DEPARTMENT**

**REPORT**

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To: Mayor Darrell R. Mussatto and Members of Council  
From: Ben Themens, Director of Finance  
SUBJECT: HARRY JEROME FINANCING STRUCTURE AND RISK  
Date: July 18, 2018 File No: 02-0800-30-0002/1

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**RECOMMENDATION:**

**PURSUANT** to the report of the Director of Finance, dated July 18, 2018, entitled, "Harry Jerome Financing Structure and Risk":

**THAT** staff continue with the design, tendering and construction of the Harry Jerome Community Recreation Centre (HJCRC) and negotiation of a land lease agreement for the Harry Jerome Neighbourhood Lands (HJNL) with Darwin Properties for financing the project;

**THAT** the Community Amenity Contributions of 150 East 8th Street and the proceeds of the density sale (excluding Block 62 density) to 1441 St. Georges Ave be set aside and allocated in the following order of priority:

1. funding of the HJCRC and HJNL projects, net of Tax Sale Land Reserve Fund and British Columbia Municipal Financing Authority borrowing;
2. any excess funding to be used for the construction of 37 space childcare or 80-unit non-market housing at the HJNL site; and
3. unused funding of 150 East 8<sup>th</sup> Street to be allocated 80% to the Civic Amenity Reserve Fund and 20% to Affordable housing Reserve Fund and unused funding of density sale revenue to be allocated to the Civic Amenity Reserve Fund;

**THAT** staff be authorized to make arrangements in a timely manner, to secure \$90 million bridge financing from the British Columbia Municipal Financing Authority for the purpose of funding the tender and construction of HJCRC project;

**THAT** staff be authorized to internally borrow \$20 million in bridge financing from the Tax Sale Lands Reserve Fund for the purpose of funding the tender and construction of HJCRC project;

**THAT** staff implement the risk mitigation measures as set out in the report;

**THAT** (Funding Appropriation #1826) an amount of \$4,125,000 be appropriated from the Civic Amenity Reserve Fund (Harry Jerome Project fund) for the purpose of funding the HJCRC project oversight, detailed design and construction;

**THAT** (Funding Appropriation #1825) an amount of \$3,000,000 be appropriated from the Civic Amenity Reserve Fund (Harry Jerome Project fund) for the purpose of funding Silver Harbour Seniors' Activity Centre interim moves, rent and Tenant Improvements;

**THAT** (Funding Appropriation #1824) an amount of \$6,500,000 be appropriated from the Civic Amenity Reserve Fund (Harry Jerome Project fund) for the purpose of funding the detailed design and construction of the relocated Lawn Bowling facility;

**THAT** the September, 2018, City Revised Budget consider an allocation of \$6,125,000 for the purpose of further funding the HJCRC project oversight, detailed design and construction;

**AND THAT** should any of the above amounts remain unexpended at December 31, 2024, the unexpended balances shall be returned to the credit of the respective fund.

## **PURPOSE:**

This report discusses the financing of the Harry Jerome Community Recreation Centre (HJCRC) project through the lease of City lands on the south side of East 23<sup>rd</sup> Street between Lonsdale and St Georges, the Harry Jerome Neighbourhood Lands (HJNL).

The report also aims to further follow-up on the June 26, 2017 Council resolution requesting that staff be directed to proceed with the schematic design of the new HJCRC as follows:

“6. Investigation of interim financing solutions to fund construction of the HJCC prior to the commencement of construction of the development lands south of 23rd Street”

The report also discusses the risks related to the financing of the project over the next six years. It is important to note that with the exception of the amount spent on design of the HJCRC and reimbursement of rezoning and request for proposal (RFP) preparation costs to Darwin if the City was to cancel the project, the City has limited risk exposure until it enters into firm agreements for the construction of the HJCRC and HJNL.

## **BACKGROUND:**

The City of North Vancouver issued an RFP in July, 2017 for the “Acquisition and Development of City Lands” located on the south side of East 23rd Street between Lonsdale and St Georges. The RFP invited proponents to submit offers for 90 or 75 year long term lease or a fee simple purchase. The RFP stipulated that the lands would be acquired for the purpose of multifamily residential and mixed development in the range of approximately 500,000 square feet.



Following a review of the offers, Council adopted a resolution authorizing staff to negotiate with Darwin Properties an agreement to lease the lands for a 99-year period. Such a lease term is anticipated to generate approximately \$210 million contribution to the City. It is worth noting that the amount is an estimate that may fluctuate, as it is dependent on the overall density contemplated and approved by Council as well as market pricing adjustments.

Rezoning of the lands is complete and negotiation to finalize the land lease and development phases are progressing well.

Preliminary design of the HJCRC is also progressing well. Based on the Schematic Design, a Class 'C' estimate has now been completed. HJCRC costs are higher than initially anticipated; increasing financial risks but remaining within funding provided from the HJNL.

## **DISCUSSION:**

The contemplated financing structure of the HJCRC project and HJNL transaction creates some risks for the City. The principal purpose for developing the HJNL is to raise sufficient funds to help enable the construction of the new HJCRC. This will be the primary objective of the efforts and the revenue generated from the HJNL transaction should go to this amenity in priority. The proposed HJCRC project includes several significant components such as an aquatic centre with a 50 M pool and leisure pool, an arena, a curling facility, multipurpose spaces, fitness centre and gymnasium as well as sports courts and walking track on the roof of the Centre. The new Centre must be developed with an appropriate amount of parking and also provide space to accommodate the Silver Harbour Seniors' Activity Centre who will be relocated from their existing location which is scheduled for redevelopment as part of the Darwin land transaction.

Other items that potentially are to be funded from the land transaction include:

- Relocation of the North Vancouver Lawn Bowling Club to the Mickey McDougall site including construction of a new lawn bowling club and greens;
- Construction of a new park including a walking route and new public open space in the HJ development lands to partially offset the loss of the Norseman Field;
- Construction of a section of the Green Necklace through or around the HJ development lands; and
- Construction of a temporary skatepark.

As part of the project, Council also requested that staff consider the inclusion of non-recreational city amenities and improvements on the site including non-market housing units and a childcare. Finally, it is important to note that no capital improvement related funding has been set aside for Flicka Gymnastic.

### ***Project Pricing Risk***

Based on Class 'C' estimate of the HJCRC, the current cost of the project, excluding non-recreational city amenities, is estimated at approximately \$237 million and is broken down as follow:



**Table 1 – Project Preliminary Estimate**

**HJCRC Land Development amenities**

HJCRC Class C estimate incl. silver harbour	\$ 200,692,000	
Lawn Bowling relocation	} } }	
Silver Harbour (Relocations, TI's, Rent)		\$ 9,850,000
Temporary Skatepark		
<b>Sub-Total:</b>	<b><u>\$ 210,542,000</u></b>	

**Non-recreational amenities and improvements**

Park Redevelopment	\$ 6,500,000
Non-market housing units (80 units)	\$ 15,400,000
Childcare (37 spaces)	\$ 5,000,000
<b>Sub-Total:</b>	<b><u>\$ 26,900,000</u></b>
<b>Total:</b>	<b><u>\$ 237,442,000</u></b>

The HJCRC estimate of \$201 million includes approximately 400 parking stalls. The amount also includes approximately \$32 million (22% of the \$144 million construction cost) for contingencies and cost escalation. There is significant uncertainty with regard to cost escalation given recent construction/tender pricing increases. The City will only be in a position to affirm the project price at the time of contract tendering and to decide at that time whether to proceed with that price or to implement mitigation measures before awarding a contract. After the award of the contract, any cost escalation risk (excluding project contingency risk) will be borne by the private contractors. This risk could be further mitigated by adjusting the project scope.

At this time, on its own, anticipated HJNL funding is insufficient to fund the non-recreational amenities. The current cash flow model considers using Parks DCC funding to fund the park redevelopment. Park DCC's may be used to fund approximately 50% of eligible park construction costs. Other amenities should be deferred to a latter phase of the project to reduce risks of a shortfall if the tendered price of the HJCRC project comes over the Class "C" estimate as well as to allow the identification of other funding sources. For instance, Harry Jerome dedicated funding that has been set aside in the past six years may provide a surplus that could be used to fund non-recreational amenities near the end of the project. Funds from the Affordable Housing Reserve, which are anticipated to grow significantly in the coming years from potential development activities, could also offset the cost of the non-market housing. Delaying the implementation of non-market housing will also provide the opportunity to assess and adjust for the impact, if any, on the affordability of residential units built on leased land. It is expected that a long-term land lease could result in discounted residential unit pricing.

The March 8, 2018, report to Council suggested that developer's Community Amenity Contributions (CACs) or density sale (excluding from Block 62) of two Council approved developments (150 East 8th Street and 1441 St. Georges Ave.) be included in the HJCRC funding budget to enhance the project contingency reserve. Once construction cost is confirmed, unrequired funding from this source could be allocated in priority to fund non-recreational amenities if needed or returned to usual CAC's allocation reserves (80% Civic



Amenity Reserve Fund and 20% Affordable Housing Reserve Fund) or density sale related reserve, the Civic Amenity Reserve Fund.

At this time, the review does not consider potential external contributions from the Federal Grant program or that may be forthcoming from development activities in other areas of the City as well as potential additional revenue that could be generated through the sale of other City-owned lands. Developer's CACs could generate significant revenue in the Civic Amenity Reserve Fund which could be used to mitigate cash flows issues. Such funding is subject to approval of major development applications by Council, economic fluctuations and project scheduling. While such funding is often used by Planning department to enhance projects or considered in the City Financial Plan to fund projects in future years, future conditional funding of this nature is not recognized in the Plan's current year or as available to fund a project where funding certainty is required.

### ***Darwin Leasing Offer***

One of the City's due diligence steps has been to ensure that the proposed long term lessee of the development lands has the capacity to pay an amount of approximately \$210 million. The proposed lessee, Darwin, was the successful proponent further to the public Request for Proposals for acquisition and development of these lands to pay for HJCRC, and the City is currently in negotiations with Darwin on the details of the proposed land lease and development agreements. Given the potential financial consequences for the City if a lessee were to default under the terms of the Agreement once construction of the Harry Jerome has begun, the City is taking steps to understand and mitigate this risk.

For this reason, the preparation of the agreements between the City and Darwin will provide safeguards to protect the City's interests. Guarantees under the form of a deposit, letter of credit, parental company guarantee, and ownership security of various building spaces have been negotiated with Darwin and will provide some financial guarantees in case of default.

Note that if the City exercises its right to cancel the HJCRC project on the north lands and cancels any remaining phases of the long term development lease on the south lands, the City would be liable to Darwin for reimbursement of their rezoning costs and their Request for Proposal (RFP) preparation costs but not for other costs or potential economic loss.

### ***Debt Financing***

The City is setting aside an amount of \$2.6 million per year for the HJCRC project. It has been assumed that this amount could be used to offset the cost of debt reimbursement once the project is completed. Based on latest interest rate increases, staff estimate that an annual debt reimbursement of \$2.6 million would allow the borrowing of an amount of approximately \$50 million. Based on the fact that interest rates could increase further in the coming years, staff recommends that a conservative debt amount of \$45 million be considered in the financial modeling. Furthermore, as discussed below in the section discussion operation and maintenance costs, staff recommend minimizing the size of a long-term capital loan to offset the additional operation and maintenance cost of the larger facility.

To meet Council's requirement for interim financing solutions to fund construction of the HJCRC prior to the commencement of construction of the HJNL, staff could arrange construction borrowing during the project. At this time, the cost of the interest has not been considered in



the project cash flow. While construction-borrowing arrangements will be required to allow tendering, it is unclear if funding of this source will actually be required to fund construction. It is also important to note that based on current rates and City revenue, City residents approval through a referendum or an alternative approval process would be required if an amount in excess of \$90 million needs to be borrowed.

**Cash Flow Analysis**

The development of the cash flow and financing options for this project is challenging given the level of risk and uncertainty. It is important to note that there are two aspects with regards to the financial needs of the projects. First, the City must have sufficient funding to cover expenses upon receipt of invoices. However, a second, more stringent aspect is that funding needs to be in place prior to project tendering.

This translates into having solid financial agreements in place prior to tendering. For instance, staff considers that if the project is to be funded with a loan, the loan should be in place before tendering. Taking this into consideration, staff has made some assumptions with regard to the scheduling of the project's tendering and created a financing scenario. The results are summarized in the following table. The table includes assumptions regarding Darwin's lease payments on the basis of the agreement currently under negotiation.

**Table 2 – Annual Cash Flow Summary Forecast**

**Estimated Cash Flow Summary (in million \$)**

	Total	2018	2019	2020	2021	2022	2023
<b>Financing Need - Project Tendering</b>	\$ 237.4	\$ 19.8	\$ 15.6	\$ 157.3	\$ 8.9	\$ 15.4	\$ 20.4
HJCRC Design, Project Oversight and Constructio	\$ 200.7	\$ 10.3	\$ 15.3	\$ 157.3	\$ 2.4	\$ 15.4	\$ -
Lawn Bowling relocation	\$ 6.5	\$ 6.5	\$ -	\$ -	\$ -	\$ -	\$ -
Silver Harbour (Relocations, TI's, Rent)	\$ 3.0	\$ 3.0	\$ -	\$ -	\$ -	\$ -	\$ -
Temporary Skatepark	\$ 0.3	\$ -	\$ 0.3	\$ -	\$ -	\$ -	\$ -
<i>Non-recreational amenities and improvements</i>							
New park	\$ 6.5	\$ -	\$ -	\$ -	\$ 6.5	\$ -	\$ -
Non-market housing units (80 units)	\$ 15.4	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 15.4
Childcare (37 spaces)	\$ 5.0	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 5.0
<b>Funding Sources</b>	\$ 255.0	\$ 27.7	\$ 53.0	\$ 112.6	\$ 73.4	\$ 2.6	\$ (14.3)
Civic Amenity Reserve	\$ 24.4	\$ 14.0	\$ 2.6	\$ 2.6	\$ 2.6	\$ 2.6	\$ -
Contributions - 2 Projects (CAC and Density Sale)	\$ 13.7	\$ 13.7	\$ -	\$ -	\$ -	\$ -	\$ -
Park DCC Reserve	\$ 3.2	\$ -	\$ -	\$ -	\$ 3.2	\$ -	\$ -
Darwin - 3 phase payments	\$ 213.7	\$ -	\$ 50.4	\$ -	\$ 87.6	\$ -	\$ 75.7
MFA Borrowing	\$ -	\$ -	\$ -	\$ 90.0	\$ -	\$ -	\$ (90.0)
Internal Borrowing	\$ -	\$ -	\$ -	\$ 20.0	\$ (20.0)	\$ -	\$ -
<b>Cumulative Annual Excess Funding</b>	\$ 17.6	\$ 7.9	\$ 45.3	\$ 0.6	\$ 65.1	\$ 52.3	\$ 17.6

Based on a 2020 HJCRC project tendering, a significant funding shortfall would occur that year. The scenario assumes that the City will arrange for a \$90 million loan, the maximum amount available without going through a referendum or an alternative approval process. The City will also adopt a resolution to provide \$20 million through internal borrowing from internal reserves, mainly the Tax Sales Land Reserve Fund. This will provide \$110 million of funding to allow project tendering with a surplus of less than \$1 million. The borrowing is expected to be reimbursed (\$20,000,000) in 2021 and (\$90,000,000) in 2023 with proceeds from the Darwin



land lease. Most of the amount advanced by the City should be considered as bridge financing until final property transfer to Darwin.

The review of the above table provides the following information:

- 1) The City should make arrangements to borrow \$90 million and allow internal borrowing of \$20 million by 2020, for interim construction financing until Darwin takes possession of the various phases, to allow the project to proceed. The project cash flow defers \$15 million for the purchase of some of the interior fit-out items in 2022 to better match cash outlays with expected funding receipt. As an alternative, the HJCRC project could be (1) tendered and/or built in further phases, or (2) delayed by one or two years, noting that phasing of the project may be limited by the fact that underground parking should ideally be built in one phase and that construction prices have been increasing steadily for a number of years.
- 2) The project should only proceed if an initial contribution of at least \$50 million is provided by Darwin prior to project tendering.
- 3) The proposed scenario would not leave much room to accommodate substantial cost overruns. The tendering and construction of the project could be compromised if prices quoted by contractors turn out to be above budget estimates.
- 4) If needed, the available funding could potentially be increased by \$15 - \$20 million if the childcare and non-market housing components are excluded from the project or, alternatively, if childcare is provided by a for-profit entity at reduced City cost and non-market housing is funded from the Affordable Housing Reserve Fund.
- 5) The forecast anticipates that the project could be completed with \$17.6 million in excess funding. The excess funding should be kept as a contingency fund and used for other purposes only following project completion. The recommendation proposes that any excess funding be used in priority to restore the Community Amenity Contribution of 150 East 8th Street and the proceeds of the density sale to 1441 St. Georges Ave.
- 6) The model assumes that the City reimburses the \$90 million MFA loan in its entirety. The interest and long-term loan repayment savings could provide additional operating funding to cover the potential increase of the new Centre operation and maintenance costs.
- 7) Table 2 aims to ensure that financing will be available for tendering purposes. Actual disbursements will occur only once work or products have been delivered. Assuming no issues/delays regarding the Darwin agreement, it is likely that some of the funding provisions included in the table will not be used to their full extent.
- 8) Ultimately, there could be a substantial pricing differential if the City was in need of seeking a new HJNL purchaser as market conditions cannot be predicted, and revenues will fluctuate with values at time of land transfer. Some guarantees have been requested from Darwin to mitigate risk in this regard.



### ***Risk Mitigation***

This report has identified a number of risks. If Darwin or any developer were to default at any stage after the first phase on the development lands, the City has identified a number of factors to mitigate the risk to the City. For this reason, the preparation of the agreements between the City and Darwin will provide safeguards to protect the City's interests. This is important. For example, in the absence of sound mitigation in the agreements, if Darwin was to default on the agreement or substantially delay payments, the project could be delayed and/or the City could find itself significantly in debt with little or no available funding in its Tax Sales Land Reserve Fund. The City would cease receiving annual interest revenue from the Tax Sales Land Reserve Fund to fund some of its capital projects. Furthermore, in the event of lease payment default, the City would need to increase taxes by approximately 6% to pay an estimated \$5 million annually in principal and interest on a potential \$90 million loan.

Many of the risks identified in this report should be expected in a project of this magnitude. Accordingly, the Recommendation on page 1 of this report recommends to continue with the design, tendering and construction of the Harry Jerome Community Recreation Centre and discussion of a land lease agreement with Darwin Properties. However, the Recommendation also directs staff to implement the risk management measures discussed in this report.

Given the size of this project in comparison to the City relatively small financial resources, there are a number of identified project risks to mitigate. For the purpose of minimizing risks, staff have compiled the following potential measures for consideration:

- 1) set aside projected excess funding as a contingency until project completion and prioritize allocation of HJNL proceeds to refunding the project debt;
- 2) phase project to match revenue and expenses as much as possible;
- 3) defer optional non-recreation amenities included in the Darwin agreement to a latter phase of the HJNL project;
- 4) monitor Darwin's permitting/construction/sale progression;
- 5) include disbursement deadlines in Darwin's agreement to control compliance or default;
- 6) request guarantees and/or bonding from Darwin in addition to deposits, and provide for City resumption of the pre-zoned and subdivided and serviced future phases of the lands in the event of any default;
- 7) identify additional funding sources e.g. CAC's, Affordable Housing Reserve, DCC's and surplus land sales;
- 8) Convert part of the MFA bridge financing into a long-term loan (this may reduce funding availability to fund operation and maintenance cost of the new HJCRC); and/or
- 9) Seek senior government funding such as Federal Grant Program.

### ***Operation and Maintenance Cost – Impact on Debt Financing***

It is important to note that preliminary cost estimates indicate that the operation and maintenance (O&M) cost of the proposed new HJCRC will be approximately \$1.4 million more than the current Centre. There currently is no provision for O&M cost increases in the City budget and there is uncertainty with regard to the District of North Vancouver cost sharing contribution. However, at this time, considering the fact that the current funding scenario of the project is not anticipating the use of long-term debt, the amount set aside annually for the construction of the new HJCRC will suffice to fund anticipated additional O&M costs. This being

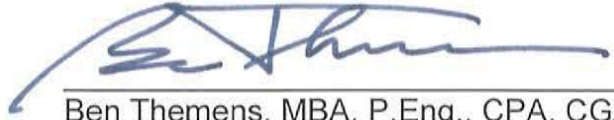


said, Council may want to consider the implementation of pay parking to allow the recovery of some of parking related costs.

**INTER-DEPARTMENTAL IMPLICATIONS:**

This report has been prepared with the assistance and information received from the Strategic Initiatives & Services and Planning departments. The report has been reviewed by the Major Project Team on July 17, 2018.

RESPECTFULLY SUBMITTED:



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