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INDUSTRY REGULATION AND COMPETITION POLICY

Buildings with Benefits: The Defect of Density Bonusing

by
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- Under section 37 of Ontario's *Planning Act*, municipalities can implement a form of "density bonusing," a practice whereby municipalities secure "benefits" from developers in return for allowing them to construct buildings that exceed height and density restrictions. Once confined to large office buildings in Toronto's central business district, the use of density bonusing has grown throughout Ontario, as it has throughout Canada. This growing popularity is unfortunate, however, as the practice is often arbitrary and opaque, and based on weak rationales for its use.
- In light of the current Ontario government's drive to address the flaws in the province's planning regime, it should at least drastically rewrite the legislation governing density bonusing to ensure a more transparent process. Alternatively, the province could repeal section 37 altogether, as even the most structured and transparent implementation of density bonusing continues to rely on weak rationales for its use in urban planning.
- Municipalities have better tools to achieve more useful and equitable outcomes. The province of Ontario, and other jurisdictions in Canada, should consider such tools in place of density bonusing.

Since 2015, Ontario has embarked on an ambitious and much needed overhaul of urban planning legislation and institutions in the province. Recent changes include, first, a prohibition, albeit watered down, on applications to amend official plans for the first two years after they come into effect; second, the introduction of inclusionary zoning to the repertoire of tools available to municipalities to address housing affordability issues; and, third, the introduction of community planning permits to simplify the development process.

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These changes signify recognition on the part of the provincial government that the existing institutions and legal framework that govern planning in the province are inadequate to address a rapidly urbanizing population and the massive construction boom in its largest cities. Despite all these changes, however, one relic of the past planning regime remains: section 37 of *Ontario's Planning Act*. This provision allows municipalities to implement a form of “density bonusing,” a practice whereby municipalities secure “benefits” from developers in return for allowing them to construct buildings that exceed height and density restrictions. Once confined to large office buildings in Toronto’s central business district, the use of density bonusing has grown throughout Ontario, as it has throughout Canada. This growing popularity is unfortunate, however, as the practice is often arbitrary and opaque, and based on weak rationales for its use.

In Ontario, section 37 agreements are usually negotiated on an ad hoc basis, with the value of the benefits negotiated behind closed doors. Although the nature of the benefits municipalities secure from developers can involve community consultation and significant input from city staff, they are just as often determined by elected officials, with limited input from residents or city workers. In light of the current Ontario government’s drive to address the flaws in the province’s planning regime, it should at least drastically rewrite the legislation governing density bonusing to ensure a more transparent process. Alternatively, the province could repeal section 37 altogether, as even the most structured and transparent implementation of density bonusing continues to rely on weak rationales for its use in urban planning.

Understanding Density Bonusing in Ontario

Section 37 (1) of Ontario’s *Planning Act*, 1990, states: “The council of a local municipality may, in a by-law passed under Section 34, authorize increases in the height and density of development otherwise permitted by the by-law that will be permitted in return for the provision of such facilities, services or matters as are set out in the by-law.” The *Act* further states that municipalities may employ this power only if they make explicit provisions for it in their official plans. As of 2015, the *Planning Act* also stipulates how money collected from developers must be invested by municipalities, ensuring that the funds are used for their explicit purposes. Beyond these provisions, the *Act* contains no guidelines on exactly what is intended by “facilities, services, or matters,” nor does it explain how municipalities should implement or employ this tool of planning. In addition, there are no provincial regulations or other pieces of legislation that stipulate the intent and purpose of section 37. The only provincial document to address the use of section 37 is a one-page “information sheet” now rendered into a webpage on the Ministry of Municipal Affairs website (Ontario 2009). This information sheet appears to be the province’s last word on the subject of section 37. It does little, however, to illuminate the purpose of section 37 or how municipalities should implement it. The sheet suggests the following possible uses for section 37: public art, or transit improvements; anything supporting the likes of community development or intensification; and desirable visual amenities – the latter proved to be the most popular “benefit” the City of Toronto secured from developers from 2007 through 2011 (Moore 2013, 2016).

In the absence of provincial guidelines, municipalities have interpreted and implemented section 37 as they see fit. As the municipality with the longest history of using the section, Toronto’s established practice for securing section 37 agreements has largely shaped its use elsewhere, although its application does vary somewhat. Toronto, concerned that the courts might consider a highly structured approach to section 37 beyond the authority of the municipality – even though no Ontario court has ever rendered such a decision – has implemented a system where the values of most section 37 agreements are negotiated with developers on an ad hoc basis (Toronto 2007). This approach has resulted in an opaque process in which these values are largely

determined by developers and city planners behind closed doors, and has led, at times, to a lack of coordination in determining what benefits to secure from developers. Prior to 2010-2011, when an enterprising city planner began compiling a comprehensive list of all section 37 agreements, the absence of coordination often resulted in funds secured from developers going unspent for years.

Toronto does allow for a more formulaic approach under secondary plans – plans that guide development in specific neighbourhoods – suggesting it believes the courts would accept a provision that applied to only a small portion of the city. Where such provisions exist, the city determines the value of the benefits using a fixed-rate formula. Secondary plans may also specify the nature of the benefits the city will secure from developers (Toronto 2007). This approach significantly increases transparency, but, as noted, applies only in limited areas of the city. Ottawa applies such a fixed-rate system in two zones that encompass the entirety of the city’s downtown, but it still largely negotiates the agreements on a case-by-case basis because, according to the city’s own guidelines, “a standardized approach that is a rigid, value-based formula may constitute an illegal tax” (Ottawa 2017, 9). The fact that neither Toronto nor Ottawa feels comfortable implementing a transparent approach to section 37 across the entire city reflects the vague nature of this tool. Legislation enabling density bonusing in other Canadian jurisdictions, such as British Columbia, allows for a far more formulaic and transparent approach to its implementation (Moore 2013, 2016).

Many other cities in Ontario have implemented section 37 agreements through their official plans, but few deviate significantly in their practice from that of Ottawa and Toronto. For instance, although the City of Vaughan applies an explicit formula for estimating the base value of property and the value of the increased density, along with a protocol to address disputes, the value and nature of benefits secured through section 37 agreements are still negotiated on a site-specific, ad hoc basis (Vaughan 2015). Mississauga deviates even less from Toronto’s practice; its guidelines state that “the amount or value of the Community Benefits in relation to the value of the density or height increase will vary from project to project, as a standard City-wide calculation is not imposed” (Mississauga 2012). When determining the portion of the “uplift” – the value of the additional density – that the city should secure from developers in the form of community benefits, Mississauga permits a wide range between 20 and 40 percent (Mississauga 2012), allowing for significant deviation among developments.

The Origins of Density Bonusing

There is little research into the emergence and history of density bonusing in Canada. In Ontario, municipalities employed density bonusing on an ad hoc basis well before the province formally introduced the planning tool in the *Planning Act* in 1983 (Pantalone 2014). Why municipalities began adopting the practice and on what basis are unclear. According to Pantalone (2014), the province’s adding the practice to the *Planning Act* simply codified what municipalities had already been doing, which might explain why section 37 – and its predecessor, section 36 – remained so vague.

The fact that municipalities were implementing density bonusing without sanction from the provincial government also might explain the very ad hoc nature of the process. Until the early 2000s, Canadian courts, following the decision in *Ottawa Electric Light Co. v. Corporation of Ottawa (1906)*, were quick to rule as *ultra vires* any municipal decision that did not fall under its authority as explicitly stated in provincial legislation. Given the courts’ stance, it is not surprising that municipalities would avoid implementing a more transparent and structured process for density bonusing. The province of Ontario, by simply codifying existing practices in 1983, likely did little to assuage fear that the courts would strike down a more structured approach in cities such as Toronto.

The province could quickly solve Ontario cities' dilemma by explicitly allowing for a broad-based formula for the implementation of density bonusing, as British Columbia has done. The bigger issue, however, is that the arguments in favour of density bonusing are defective on a number of grounds, ultimately resulting in a highly flawed planning tool, regardless of its legal underpinning. First, when municipalities rely on density increases to justify securing benefits from developers, they are maligning density. For residents opposed to high-rise infill developments in their neighbourhoods, this might seem fair; however, although density can result in negative externalities, such as congestion, it also combats sprawl and typically leads to efficiencies in service delivery. As a tax can lead to suboptimal distribution of goods and services, so too can density bonusing unintentionally affect development.

Second, there is no explicit rationale for the use of density bonusing in Ontario. Toronto's section 37 guidelines explicitly state that a development proposal, regardless of the inclusion of a section 37 benefit, must constitute good planning (Toronto 2007); Mississauga, Ottawa and Vaughan have similar clauses in their respective guidelines (Mississauga 2012; Ottawa 2017; Vaughan 2014). This provision seems obvious: if, by employing section 37, the city was allowing bad planning, then the whole intent of the tool would be undermined. But if the planning rationale for a development is sound, then how can the municipality justify the restrictive zoning that allowed for the density bonusing in the first place? Are not the intentions of zoning by-laws and restrictions of density and height to ensure good planning?

Again, the province of Ontario could address these issues by explicitly stating the purpose of density bonusing in the *Planning Act*. Such a change, along with amendments allowing for a formulaic approach to implementing the practice, would address significantly the opaqueness of section 37. However, none of the traditional rationales behind density bonusing provides an adequate argument for its use in place of other, fairer and more transparent planning tools.

Rationalizing Density Bonusing

The primary rationale for density bonusing is known as “sharing the wealth” (Moore 2013). Its proponents argue that developers receive an unearned “windfall” profit – or, more properly, increased economic rent – when municipalities allow them to exceed density and height restrictions; therefore, they should share some of the windfall with the municipalities and their residents (Biggar 2017). This argument seems to have emerged first in the United States in the 1960s, where municipalities used it successfully in the courts to justify the practice of securing affordable housing through density bonusing in jurisdictions where the state prohibited the use of inclusionary zoning (Benson 1969; Fox and Davis 1975). At its roots, “sharing the wealth” is primarily an argument for “taking” from developers.

Such a broad interpretation of density bonusing would allow municipalities to pool funds raised through section 37 to address citywide needs, such as affordable housing. Although cities do secure affordable housing through the section, the province's 2015 changes to the *Planning Act* currently limit how municipalities can use the funds. Section 37 agreements must state explicitly what amenities will be provided through the agreement and where, and the funding must be used only for those amenities. These restrictions effectively prevent municipalities from pooling funds for future citywide projects, even if the funds are earmarked for specific use – such as for affordable housing or community centres. Furthermore, municipalities have largely interpreted the Ontario Municipal Board's requirement that there be a “nexus” between developments and the benefits secured through density bonusing as a requirement that any benefits secured from a development be located within the vicinity of the development (Biggar 2017; Moore 2013; Pantalone 2014). The province could amend the

Planning Act and explicitly grant municipalities the right to negotiate section 37 agreements based solely on this rationale, to provide greater clarity about the purpose and use of the tool.

A number of problems emerge, however, when relying on “sharing the wealth” as the sole argument for density bonusing. First, given the fiscal constraints municipalities operate under, including requirements that they balance their operating budget each year, they would likely turn to section 37 as a means to pay for most infrastructure, thus freeing up property tax revenue for services. In effect, density bonusing would simply become another general revenue source for the city. In fact, if municipalities could use density bonusing to offset general revenue, it could encourage cash-strapped municipalities to engage in bad planning, by allowing excessive density in order to raise revenue. The 2015 amendments to section 37 in the *Planning Act* – the restriction on how municipalities can collect and spend section 37 benefits – clearly indicate that the province does not intend for the section to be just another revenue source for cities.

Second, “sharing the wealth” provides no rationale for the implementation and application of density bonusing. For density bonusing to be fair and transparent there needs to be a logic for the base density that municipalities allow developers as-of-right versus the increased density resulting from density bonusing agreements – something that is largely lacking in Ontario. That is, municipalities must base their density regulations on good planning. Absent such a rationale, there is little basis for municipalities to claim that developers are benefiting from an unearned “windfall” at one level of density, but not at another.

Clearly, density bonusing requires an additional rationale tied to urban planning. There are, in fact, two common justifications for density bonusing based on planning rationale. The first, although rarely discussed in Ontario, might well be the *de facto* rationale in the province: that density bonusing should be used to compensate neighbourhoods negatively affected by new development (Moore 2013). The common use of section 37 to secure “desirable visible amenities” and new parks for adjacent neighbourhoods certainly could reflect such a rationale. When new development in established neighbourhoods involves a significant increase in density, existing residents often perceive it as threatening their community, as it can lead to such negative effects as increased congestion or the casting of long shadows by tall new buildings over existing low-rise houses; thus, the benefits secured through density bonusing could be seen as a means to mollify residents negatively affected by new development.

From a practical standpoint, municipalities could justify their base zoning by-laws as restricting development to levels of density in keeping with existing neighbourhoods, while requiring density bonusing agreements if a project would change the character of a community and result in clear negative externalities. The increasing sophistication of planning, such as the ability to estimate the effect of new development on traffic, could provide a basis for such calculations. Unfortunately, although this rationale provides a planning basis for density and zoning restrictions relating to density bonusing, it is also highly problematic: the amenities typically secured using this rationale – new parks and desirable visible amenities – do not address any of the negative effects of new development. Furthermore, there is little evidence that such amenities appease residents whose neighbourhoods have been negatively affected by growth. The apparent prevalence of such a rationale in Toronto – or at least the evidence of it, based on the nature of benefits secured from developers (Moore 2013, 2016) – is likely a product of real and perceived constraints placed on the use of section 37, such as the Ontario Municipal Board’s “nexus” requirement. It could also be the result of the direct involvement of elected officials in determining the nature of benefits in cities such as Toronto and Ottawa (Teal Architects et al. 2015). Regardless of the reason for its use, since these benefits do not address the negative externalities caused by increased density, do not contribute to

better planning and are unlikely to address residents' concerns, such a rationale forms a weak basis for what is nominally a planning tool.

The second, and stronger, planning rationale for density bonusing is rarely employed in Ontario, although it has grown in use in other provinces, such as British Columbia: that density bonusing should be used to secure contributions from developers to build citywide infrastructure necessary to accommodate increased density. The type of infrastructure built using such funds needs to be distinct, however, from development charges. The latter are intended to address the cost of infrastructure such as sewers, roads and schools necessary to accommodate new development, so there is little justification for using density bonusing to address the infrastructure needs that result from individual developments. Rather, density bonusing could be used to pool funds for large, citywide infrastructure projects, such as the construction of new transit lines. Such a rationale is in line with the Ontario government's information sheet on section 37, which explicitly mentions "transit improvements" as a potential benefit that municipalities can secure from developers.

Improved transit infrastructure is often necessary to accommodate higher-density development. At the same time, proximity to good transit can increase demand and prices for property and housing in a given area. Thus, developers can benefit from investment in transit. Using such a rationale, base zoning would allow developers to construct buildings as-of-right as long as they did not significantly affect the capacity of existing transit systems (or roads). If new development would strain such systems, municipalities would capture some of the "windfall" that developers would recoup from the additional density to help pay for the expansion of transit. The British Columbia government and municipalities in Greater Vancouver are currently investigating such an approach to funding transit (Kelly and Enta 2016).

The main problem with such an approach is that it amounts to little more than a – possibly punitive – area-specific tax on new development. Developers and new residents are not the sole beneficiaries of improved transit, but through density bonusing they would pay a disproportionate amount of the cost. It is not unreasonable for new development on existing or proposed transit lines to contribute to the improvement or construction of a line. However, as all property owners along the path of the transit line would benefit from the improvements, it is unreasonable for the builders and residents of new developments that exceed density restrictions to bear the majority of the cost. More important, although such a rationale does provide a sound planning basis for density bonusing, other tools can achieve the same goal without the level of complexity inherent in density bonusing. For instance, Ontario could allow municipalities to apply an area or citywide tax specifically for transit investment, as is common in California.

Concluding Thoughts

The main problem with density bonusing, whether or not applied in Ontario's opaque, ad hoc nature, is that the social justice argument behind "sharing the wealth" does not provide a planning tool that is fair and transparent in its application. In effect, this rationale states that if, and only if, a development exceeds the municipality's arbitrary density restrictions can the municipality share the developer's "windfall." In practice, however, municipalities can grant a "windfall" to developers just by allowing them to develop land – that is, by allowing them to do something they otherwise would not have done, leading to increased profit. Why, then, should increases in density be the only time that municipalities exert their right to sharing these "windfalls"?

Given the problems with basing density bonusing solely on "sharing the wealth" and the weakness of existing planning rationales for density bonusing, continuing its use in Ontario would be of little benefit to residents or

to the development industry, even if the province were to address the ad hoc and opaque nature of its practice. Municipalities have better tools to achieve more useful and equitable outcomes. The province of Ontario, and other jurisdictions in Canada, should consider such tools in place of density bonusing.

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