Bridging the Gap: Policy Instruments to Encourage Private Sector Provision of Affordable Rental Housing in Alberta

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Résumé

Mots clés: Alberta, des logements de location abordable, secteur privé, instruments politiques, planification
Bridging the Gap: Encouraging Private Provision of Affordable Rental Housing

Abstract
In the context of growing shortages of affordable housing in Alberta, the policy discourse in the last decade has centered on ways to get the private sector involved through a variety of public-private partnerships, policy incentives and regulatory measures. This research explores alternatives for private sector engagement in the provision of affordable housing focusing on four clusters of policy instruments—regulatory/planning, fiscal, financial and institutional. The article provides a much-needed overview of challenges and opportunities in Alberta using conceptually appropriate analytical framework, fresh empirical evidence, case study analysis and insights from the practical experiences of industry professionals. It argues that a much more robust and sustainable system of direct subsidies is required to bridge the funding gap between the cost of development and potential revenue generation in affordable rental housing. In addition to fiscal support from senior governments and improved access to more affordable long-term finance, it suggests that municipalities can play a significant role in facilitating private sector involvement by creating a positive planning and policy environment. Key recommendations in that regard focus on density bonusing, streamlined development approval and acquisition of land through land trusts and land leases.

Key words: Alberta, affordable rental housing, private sector, policy instruments, planning

1 INTRODUCTION
The withdrawal of federal funding in Canada since the mid-1990s has resulted in rapid decline in the supply of new rental housing by different providers. The responsibility has been downloaded to lower levels of government with limited resources to respond to a housing crisis. Recognising the widening gap between the limited supply of affordable rental housing and the growing need across Canadian cities, the federal government committed $680 million towards new programs over five years in 2001, another $320 million in 2002 and an additional $1.6 billion in 2005. Further $2 billion was included in Canada’s Economic Action Plan of 2009. The funding has been allocated to the provinces, responsible for the design and program delivery of affordable housing, with a requirement to match federal contributions (CMHC, 2009). In Alberta, federal funding of $98.62 million under the Affordable Housing Partnership Initiative (AHI), has resulted in 3,683 units as of September 2007. The partnership was extended with additional federal funding of $119 over three years and another $386 million in 2009. A new plan of the government of Alberta, approved in 2009, aims at ending homelessness
in 10 years by committing $1.2 billion in capital investments and $2 billion in operating funding. The plan, based on the “housing first” approach, is expected to create 11,000 affordable housing units by 2012, mostly supported through AHI and other municipal initiatives (Housing and Urban Affairs, 2011). Alberta’s plan—the first of its kind among Canada’s provinces and territories—builds on the momentum of growth in affordable housing investments by municipalities and the province in recent years (AAHTF, 2007; City of Edmonton, 2007; Stubbs et al., 2007).

This much-needed provincial government response aims at providing a range of affordable housing opportunities along the continuum—from emergency shelters, to transitional housing, to non-market rental (social or subsidised housing), to affordable rental (near market) housing and affordable homeownership (AAHTF, 2007). The target group is admittedly broad—from homeless and vulnerable households in need of supportive housing and services (e.g. people with addiction and mental health problems), to low-income people, key workers, immigrants and large families facing affordability problems in local housing markets. Recently Alberta has experienced high population growth (over 10%), low vacancy rates (less than 1%), some of the highest rent increases in Canada (4-5 times the national average), rapid increase in house prices, and a significant growth of households in core housing need (over 106,000 more compared to 2001). A growing economy, coupled with housing supply shortages, has brought scarcity of affordable housing to the forefront.¹ The Provincial Affordable Task Force called for urgent attention to supply-and demand-side responses to a housing crisis, reinforcing the message in the municipal housing strategies (AATF, 2007; City of Calgary, 2008; City of Edmonton, 2007). Some of the key recommendations have focused on regulatory reforms, better integration of plans and policies and partnerships between different levels of government, the private and non-profit sector to deliver affordable homes. Municipalities have responded with their own initiatives, such as The 10-year Plan to End Homeless in Calgary, Edmonton’s Cornerstone Plan and The Community Plan on Homelessness and Affordable Housing for the Regional Municipality of Wood Buffalo. These plans emphasised the following: i) more effective partnerships with senior governments for sustainable capital funding, ii) leverage of corporate and private sector contributions, iii) municipal leadership and more effective planning solutions to provide affordable housing through the entire housing continuum.

Within this context of commitment by the three levels of government, most of the new affordable rental housing in Alberta is built by the non-profit organizations and social landlords (public organizations). However, policy documents by the provincial and municipal governments emphasize the need to get the private sector involved through a variety of public-private partnerships, policy incentives and regulatory measures (AAHTF, 2007; City of Edmonton, 2007). The Housing Capital Initiatives Grant Program finances up to 70 percent of the de-
development costs, allocated on a competitive basis to municipal, non-profit and private organisations. The engagement of private developers in Alberta has been limited due to reluctance to provide 30 percent contribution, different role in the marketplace and a number of constraints. The private sector, just like anywhere in Canada, is profit driven. Not only is affordable rental housing expensive to build, particularly in high growth cities with increasing development costs, but due to the target consumers of low- and moderate-income households, profits are usually limited or non-existent and substantial losses might occur.

The article seeks to explore alternatives for private sector engagement in the provision of affordable rental housing. It provides a much-needed overview of challenges and opportunities in that regard using fresh empirical evidence and insights from the practical experiences of industry professionals. The article is organised in three parts. First, the objectives and methodology of the research are outlined. Second, an analytical framework is presented and applied to the evaluation of four clusters of policy instruments to encourage private sector involvement in affordable rental housing. Third, the most significant barriers in the process are outlined with a final reflection on the most important changes needed to create a more efficient response.

2 Objectives and Methodology
The research explores the most appropriate policy instruments that can be implemented to encourage the production of new affordable rental housing by the private sector. The approach provides some unique opportunities based on the ability of the sector to leverage capital and to realize efficiency gains in the development process that could contribute significantly to increasing supply of affordable housing, and compliment the efforts of other sectors. Notwithstanding the diversity of development alternatives, the private sector could lower costs through construction, design, and financing innovations. If the provision process is unpacked into stages—promote/finance, design/build, and manage/operate—recent research indicates that the private sector can handle the design/build component better, while the non-profit sector can best handle the management component (CBC, 2010). Focusing on instruments targeting private sector engagement in affordable rental housing is admittedly complex. While such instruments can be used as stand-alone interventions, they are often packaged to deliver better results in terms of quantity, adequacy and affordability of housing.

Specifically, the research has three main objectives:

- To identify barriers and opportunities for private sector involvement in the provision of new affordable rental housing in Alberta;
- To review the advantages and disadvantages of government interventions——
planning (regulatory), fiscal, financial and institutional—encouraging the provision of affordable rental housing;

- To provide recommendations on policy measures to effectively engage the private sector in the provision of affordable rental housing, particularly through the planning system.

For the purpose of this research, the term affordable housing refers to rental housing for low- and moderate-income households where the cost does not exceed 30% of household income (CMHC, 2009). More specifically, these households have income below the regional median income and may include low- and very low-income households and people with special needs (AAHTF, 2007). In the continuum of affordable housing provision, the focus is on non-market subsidised rental housing that does not necessarily target the most vulnerable households. Due to the experimental nature of private sector engagement in Alberta, projects often bridge different options (social housing, near market rental and affordable homeownership), and the divisions are not always clear-cut. Within this broader portrait, case studies feature projects developed by non-profit institutions and municipal social housing providers in collaboration with the private sector illustrating different levels of engagement in the provision process—promotion/finance, design/build, and manage/operate.

The research methodology incorporates a comprehensive literature and policy review, an environmental scan of affordable rental housing projects throughout Alberta, and key informant interviews of a range of industry professionals. The literature review includes studies and policy analysis of practices of private sector involvement in affordable rental housing provision in Canada, the United Kingdom and the United States to develop a framework for evaluation as well as to identify the advantages and disadvantages of the most promising policy instruments to leverage private sector involvement. The environmental scan consists of 17 affordable housing developments in five municipalities throughout Alberta. These include six projects in Calgary, five in Edmonton, one in Fort McMurray, three in Medicine Hat and two in Red Deer to better understand the diverse responses of the private sector in the present framework of regulatory, fiscal and financial incentives. The projects have been selected to illustrate the diversity of private sector involvement including managing and overseeing projects, financial and in-kind contributions, and building at-cost. The primary research also includes 28 key informant interviews of housing industry professionals related to the projects including real estate professionals, government personnel, and non-profit and for-profit housing providers and developers. The face-to-face and/or telephone interviews, carried out in late 2007 focused on identifying barriers and opportunities for private sector involvement in the provision of affordable rental housing in Alberta. Key informants were selected on the basis of the environmental scan.
and referrals from industry associations and municipal officials. The interviews followed an interview protocol with questions designed to elicit responses along the following line: i) experience with the provision of affordable rental housing; ii) barriers encountered; and iii) incentives and policy instruments to encourage more effective participation. Interview participants have not been named in order to maintain anonymity and confidentiality. A follow up in-depth discussion with a small sample of key informants was completed in early 2009.

3 Framework for Analysis
The research is driven by the premise that better policy environment generates more efficient responses. The analytical framework is designed to explore the relationship between housing policy instruments and the system of new affordable housing provision. The emphasis is on the mix of housing policy instruments—regulatory, fiscal and financial to encourage new supply and to deal with the front-end loaded nature of housing costs (Cramona et al., 2003; Stephens et al., 2002). These findings in the literature have influenced the design of a conceptually appropriate framework for this research presented in Figure 1. Notwithstanding the importance of demand subsidies, it focuses on policy instruments designed to generate a supply response, particularly by the private sector. In the housing policy realm, the literature documents the influence of regulatory instruments on efficiency in the production process by making affordable housing providers and developers more responsive to household preferences or reducing the costs (Cramona et al., 2003). Inclusionary zoning, planning agreements, density bonusing, land transfers and land taxes are used to extract some of the ‘excess profit’ of the landowner and/or provide incentives provide significant impetus for private involvement in new affordable rental housing (Whitehead, 2007). Planning is perceived as the most important way for governments to affect the market. It can promote levels of housebuilding in locations that maximize social welfare as well as restrict the use of land, thereby reducing the supply and increasing the cost of housing (White and Allmendinger, 2003). This is significant for developers because land is a critical component in the production of housing.

Different countries have experimented with a range of fiscal instruments requiring direct expenditures of the government (grants, subsidies, tax incentives), or indirect, such as depreciation allowances or rent control (Boelhouwer, 1997; Whitehead, 2007). Some countries subsidise a range of housing suppliers directly (with conditions on production levels and rents) reducing housebuilders’ and landlords’ costs in affordable rental housing (Mullins and Murie, 2006). These fiscal instruments operate with various levels of efficiency, transparency, and distributional equity (Tsenkova, 2009). Financial policies to enhance the performance of housing providers include monetary policies and a variety of financial instruments to ensure long-term finance and diversity of mortgage products. (Buckley
In some countries borrowing costs from private sector institutions are subsidized, borrowing guaranteed by a government agency, and/or made available at sub-market rates. Further, institutional measures are also a more indirect way for the government to influence the production of affordable housing. This includes the creation of housing and land trusts, which become independent institutions that have the capability of autonomously allocating government funds for affordable housing.

The analytical approach of the research avoids policy centrism and recognises the importance of institutional structures in defining outcomes in the provision system and diverging responses to policy intervention (Doling, 1997). Often a combination of housing policy instruments can be packaged to achieve certain outcomes and/or to improve the efficiency and the effectiveness of affordable housing providers (Tsenkova, 2009). Adding another layer of complexity, these interventions in each locality can generate a different private sector response as well as lead to different business strategies for land acquisition and capital mobilisation. The approach recognises that private sector providers are driven by market imperatives of profit maximizing to maintain their business, they use the market as the basis for important investment decisions and the analysis of cost and risk is critical for their performance (Myerson et al., 2007; Pomeroy, 2005).

4 Policy Instruments to Encourage Private Sector Provision

The private sector, primarily the development and homebuilding industry, can potentially play a vital role in the provision of affordable rental housing. Different policy instruments are used in Canada, and to some extent in Alberta, to encourage its involvement. These supply-based instruments are reviewed below using four categories—regulatory (planning), fiscal, financial and institutional—with a reference to their advantages and disadvantages (see Table 1).
4.1 Regulatory Measures

Density Bonusing allows developers to add more floor area or additional density in exchange for certain provisions that benefit the community, such as a certain percentage of affordable housing units (AAHTF, 2007). Density bonus programs allow developers to provide additional market rate units in sufficient quantity to offset the costs of the required provision of affordable housing (Taylor, 2006). By increasing the density of a project, a developer is able to provide affordable housing units without negatively influencing the revenue as the land becomes cheaper per unit (Kowalchuk, 2004). Density bonusing also provides the opportunity to mix market and non-market units within the same building thereby creating a ‘social mix’. In the City of Calgary, the first density bonusing was included in the Beltline Area Redevelopment Plan in 2006, but has not been implemented to deliver affordable housing.

Interview data suggests that the effectiveness of density bonusing as a method for encouraging greater private sector involvement is controversial among industry professionals. Some developers felt that the policy would discourage development by increasing development costs and regulations, thereby making affordable housing projects even more difficult to build. Other developers stated that a density bonusing policy would encourage affordable housing if the correct formula was used to offset increased costs. Many developers also mentioned that in order to effectively attain maximum results a density bonus policy would require mandatory and citywide implementation, thereby becoming a de facto inclusionary zoning policy. A potential benefit of a mandatory citywide policy according to many industry representatives is that it would not create inequalities and unfair competition in the marketplace, as all developments would become subject to the same standards and restrictions. Mandatory implementation of density bonusing would result in an adjusted market producing mixed developments that rely on the market-priced units to subsidize the affordable or non-market units.

Inclusionary Zoning requires a certain percentage of affordable housing in every development as a condition of approval (Taylor, 2006; Lubell, 2006). These policies are implemented as either voluntary or mandatory regulations, depending on the goals of the municipality as well as its legal jurisdiction. As a mandatory policy, inclusionary zoning can potentially increase the supply of affordable housing, provided there is a strong development environment (City of Edmonton, 2007). Inclusionary zoning policies have the ability to promote socially inclusive communities (Porter, 2004). In other words, by mixing the market and non-market units within a community, and within a building, the development generates better rent revenues, supports debt repayment and may address Not-In-My-Backyard [NIMBY] issues (Pomeroy, 2004). Since municipalities set inclusionary
| Table 1. Policy Instruments for Private Sector Engagement in Affordable Rental Housing |
|------------------------------------------|-------------------------------------------------|
| **Regulatory Measures**                  | **Advantages**                                   | **Disadvantages**                                   |
| Density Bonusing                          | • The ability to provide substantial affordable units |
|                                         | • Create a social mix within buildings           | • Reliant on developer willingness to build higher density development |
|                                         | • Minimal municipal involvement                   | • Extensive community consultation is required due to potential resistance of higher density housing |
|                                         |                                                  | • Invites speculation into “deals” between developers and municipalities |
| Inclusionary Zoning                      | • Can potentially produce significant amounts of affordable housing |
|                                         | • Facilitates socially inclusive communities      | • It is unpopular with developers and builders as it can negatively impact profit margins |
|                                         | • Most effective in conjunction with other municipal ‘bonuses’ | • Can be viewed as a barrier to growth and an interference in the market |
|                                         | • Relatively inexpensive for municipalities to institute | • The MGA does not explicitly allow inclusionary zoning |
|                                         |                                                  | • Its effectiveness decreases in low-growth areas |
| Alternative Development Standards        | • Alberta already has a positive regulatory environment for alternative development standards | • No guarantee that cost savings will be passed on to the consumer; does not necessarily contribute to affordability |
|                                         | • The concept of alternative standards is increasingly accepted in communities and professions | |
| Land Contributions                       | • Easier access to land                           | • Strong competition for government owned land |
|                                         | • Reduced land costs could potentially lower project costs | • Land leases do not generate significant amounts of short-term revenue |
|                                         | • Political benefits without providing direct subsidies | |
|                                         | • Municipalities could retain ownership of the land while increasing their assets | |
| Streamlining the Planning Process        | • Can reduce time required for development permit approval | • Consistency and flexibility are difficult to achieve |
|                                         |                                                  | • No guarantee it will make the process faster |
| Tax Incentives                           | • Targeted incentives to construct rental housing and, | • Cost savings would occur only with the submission of a developer’s income tax and therefore, will not reduce initial costs. |
|                                         | • Advantage would apply to all developers producing new rental housing. | |
| Fiscal Measures                          | • Subsidies address the funding gap and reduce the cost of each unit | • Requirements for securing grants are often extensive and confusing, which acts as a deterrent to private developers |
|                                         | • Can be used to leverage additional financing not available otherwise | • Subsidies are typically short term due to their political nature |
Bridging the Gap: Encouraging Private Provision of Affordable Rental Housing

Table 1. Continued

<table>
<thead>
<tr>
<th>Financial Measures</th>
<th>Institutional Measures</th>
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<tbody>
<tr>
<td>Reducing or Waiving Municipal Fees</td>
<td>Housing Trusts</td>
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<tr>
<td>- Could increase the production of affordable housing in high growth areas</td>
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<tr>
<td>- Easy to implement</td>
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<tr>
<td>- Cost savings are not guaranteed to be passed along to the consumer</td>
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<tr>
<td>- Savings would not necessarily be very significant</td>
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<tr>
<td>Lending and Borrowing Practices</td>
<td>Philanthropy</td>
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<tr>
<td>- Can decrease reliance on government subsidies</td>
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<tr>
<td>- Can reduce the long-term costs if interest rates are lower and portfolio is leveraged</td>
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<tr>
<td>- Potential for government guarantees</td>
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<tr>
<td>- Difficult to decrease risk without other forms of guarantees</td>
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<tr>
<td>- Requires a significant change in business practices</td>
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<tr>
<td>- Increases the amount of funding available for affordable housing projects</td>
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<tr>
<td>- Mutually beneficial for all parties involved</td>
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<tr>
<td>- Must be filtered through a charitable organization, not directly available to private developers</td>
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<tr>
<td>- Requires a significant amount of time and relationship-building to produce substantial results</td>
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<tr>
<td>Philanthropy</td>
<td>Land Trusts</td>
</tr>
<tr>
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<td>- Mutually beneficial for all parties involved</td>
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<td>- More coordinated access to government funding</td>
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<tr>
<td>- More efficient funding can attract private developers</td>
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<td>- Can use government funding to leverage additional financing</td>
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<td>- Creation of a low-interest lending arm</td>
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<td>- Decisions can potentially be political</td>
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<tr>
<td>- Difficult to secure a dedicated funding source</td>
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<tr>
<td>- Increases the amount of land available for affordable housing</td>
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<td>- Makes land easier to acquire</td>
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<td>- Reduces development costs as land is cheaper for developers</td>
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<tr>
<td>- Significant tax barriers to donating land</td>
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zoning policies, they can determine if cash can be received in lieu of building affordable units as well as the term to sustain them as affordable rental housing (Taylor, 2006). AHI requires a unit to be affordable for no less than twenty years, while Canmore has adopted a recent policy for the provision of affordable housing in perpetuity. Other municipalities have not implemented inclusionary zoning because the Municipal Government Act (MGA) governing planning does not explicitly allow for it.

Many private developers interviewed do not support inclusionary zoning policies, especially if they are mandatory, as they tend to view this as a way of forcing the consumers of market housing to pay for affordable housing. In general, inclusionary zoning was perceived to add a significant cost to a developer, especially for units targeted to low-income households. Additional instruments (subsidies) may be required to maintain affordability for such households (CBC 2010). In addition to a decline in profits and a disincentive for future develop-
ment, the implementation is limited to high-growth areas with large scale projects (Schwartz, 2006).

**Alternative Development Standards** refer to flexible planning and engineering requirements/regulations that allow for alternatives in design and construction. Examples of alternative planning standards can include reduced setbacks, and narrower lot sizes whereas engineering standards can include reduced road allowances or reduced parking requirements. For a developer, alternative development standards can reduce construction costs and allow for a more efficient use of land in affordable housing projects. However, new standards are difficult and time-consuming to implement, which may affect project costs and affordability (Pomeroy, 2004).

Alberta has a positive planning regulatory environment encouraging the implementation of alternative development standards. Within municipalities, especially within planning departments, the idea is increasingly accepted, but its implementation in planning practice for the purposes of affordable housing provision is *ad hoc*. The interviews indicated that employing alternative development standards to address affordable housing is not a desirable option for many of the industry representatives. While some industry professionals generally support the idea to create more innovative, and potentially cost-effective developments, most professionals recognize that it would not address the need for affordable housing in a sufficient manner.

**Land Contributions.** The acquisition of a suitable site for affordable rental housing is typically more difficult due to the inability to compete for land at market rates. The federal government could prioritise affordable projects in the sale or redevelopment of government land (TBOT, 2003). A unique project in Calgary illustrates this approach. Canada Lands Company, a Crown Corporation, redeveloped a federally owned military base in 2002 into an award-winning community of Cyprus Greens with an affordable rental housing component.\(^5\) Additionally, provincial policies in Alberta encourage municipalities to release under-used infrastructure land and surplus land from municipal reserves for affordable housing (AAHTF, 2007). Municipalities have the opportunity to ‘set the table’ for land acquisition, which can reduce the development costs of affordable housing projects as the example in Box 1 indicates. The project in Fort McMurray illustrates an attempt to address the housing shortage through a partnership with a private developer, key industries and provincial and municipal governments.

Municipalities can provide land for affordable housing developments through donations, sales at controlled cost, land leases or deferred land payments (CHBA, 2007). The City of Vancouver, for example, uses long-term land leases for affordable housing developments (Kowalchuk, 2004). Land is one of the most significant barriers to building affordable housing so any contributions would be critical to increasing the supply (CBC, 2010; Stubbs *et al.*, 2007).
Box 1: Fort McMurray, Eagle Ridge, 2009

With start up funding from Alberta Ministry for Seniors and Community Supports, Centron developed a 371-acre parcel of municipal land in Fort McMurray at a set land sale price of $18.5 million. The 300 affordable housing units are split into four categories based on tenant target groups and income restrictions.

1. Need-to-reside: for tenants that live and work in Fort McMurray and do not currently own;
2. Government employees: nurses, police, etc.;
3. Oil sands employees of CNRL, a partner in the project; and,
4. Oil sands employees of other companies.

All units must be kept affordable for five years in order to discourage flipping. If units are sold before the five years, restrictions are placed on the price of the unit and eligible purchasers.

Centron maintained affordability primarily through the fixed land cost, strict timelines and its ability to manage construction effectively due to knowledge and expertise. No additional subsidies were used in this rent-to-own project for key workers.

Source: Interview data

Due to the high costs of purchasing land, developers interviewed recommended that governments and municipalities offer land leases or that the federal government change the tax laws regarding land donations for affordable housing. Leasing land for affordable housing projects can potentially serve as a win-win situation as developers would be able to reduce costs, municipalities would provide a public service while maintaining ownership in the long-term, and low income residents would gain greater access to affordable housing. The drawback of using municipal land for affordable housing is that it is subject to competition for many different uses, such as parks, utilities, or parking. Affordable housing is not necessarily a high priority for land designation and it may well be the case that at the end of lease period replacement housing may have to be provided for low-income residents.
Streamlining the Planning Process. An expedited planning process can reduce the time for development approvals, which can result in reduced costs to developers as well as potential future cost savings (Pomeroy, 2004; Kowalchuk, 2006). A practical method is to create streamlined processes that incorporate flexible, but predictable regulations in order to allow for innovative projects (Kauko, 2003). This requires consistent and transparent application of planning regulations in order to remove political influence from the approvals process.

In Alberta, the MGA outlines specific requirements regarding the planning process, while allowing flexibility at the local level to achieve greater efficiency. Recent provincial and municipal policies emphasize the importance of reduced red tape, efficient approval process and timely response to reduce risk and development costs (AAHTF, 2007; City of Edmonton, 2007; Stubbs et al., 2007). However, the interview data suggest that the actual process is far from being efficient and is considered as one of the main barriers for involvement in the provision of new affordable rental housing. The City of Calgary has responded by creating a specific position within the approvals department to handle affordable housing applications (see Box 2). The Affordable Housing Coordinator is expected to expedite applications with AHPI funding, reducing processing time by 20 percent, thus increasing municipal contribution to affordable rental housing projects.

4.2 Fiscal Measures

Tax Incentives strongly affect a private developer’s decision to build affordable housing and are particularly important to encourage private investment in rental properties. Findings from the literature and our interviews consistently point out that the current tax environment is not conducive for building new affordable rental housing. The Canadian Home Builder’s Association states, “the real answer to the housing supply problem is comprehensive tax reform to address the systemic barriers to rental investment” (CHBA, 2007: p.1). The following recommendations relate to fiscal policy intervention at the national and provincial level:

1. Lowering the GST on new rental housing or allowing a full GST rebate on new rental projects to encourage more private developers to build rental housing by increasing profit margins (Ottawa Chamber, 2005).
2. Increasing the Capital Cost Allowance (CCA) to 5% for new rental housing to reduce project risk (TBOT, 2003). The CCA is a tax deduction that allows a business to claim the loss in value of capital assets due to wear and tear or obsolescence.
3. Expanding the tax-deductible soft costs within the first year of operation of new rental properties to reduce the overall cost of the rental development (CHBA, 2007). Soft costs generally include architecture and design costs, development permits and fees, and legal fees.
4. Amending section 38 of the Income Tax Act to encourage gifts of land or land and buildings to public foundations established for the purpose of providing affordable housing (TBOT, 2003). This amendment would encourage donations of land similar to the provisions for Conservation Lands as outlined in the MGA. Currently, a land donation for affordable housing results in significant income tax penalties making such donation prohibitive.

5. Reducing the property tax burden for affordable rental housing. Currently, higher property taxes can also contribute to high operating costs.

### Box 2: Calgary, Crestwood housing, 2009

Calgary Real Estate Board has built an affordable housing project, financed through their Foundation, and supported by the City of Calgary with a land donation of $7 million. The Foundation received provincial and federal funding through AHI of $6 million. The project includes 10 market and 50 non-market units, which upon completion are transferred to the municipal housing company that manages affordable rental housing. Estimated monthly rent is $295 and cannot exceed 30% of tenant’s income. The Calgary Real Estate Foundation spearheaded this project, arranging grant funding from different levels of government and fundraising of $1.5 million. With the City’s aid, they planned the project with significant amounts of community input. The planning and approvals process was streamlined to ensure timely response.

*Source: Interview data*

Most professionals interviewed clearly stated that the current tax environment is not conducive to private sector engagement in affordable rental housing. Some industry professionals stated that a GST rebate could be beneficial, but generally
acknowledged the need for grants and subsidies to meet upfront development costs as much more effective means of mobilising development finance.

**Direct Subsidies.** Regardless of any tax credits or regulatory incentives to generate greater private sector provision of affordable housing, some form of direct subsidies is required to bridge the funding gap between the cost of development and potential revenue generation (Hulchanski and Shagcott, 2004). In Alberta, the majority of direct subsidies for affordable housing are available through the *Canada-Alberta AHI* first signed in 2002. The capital grants for a continuum of affordable housing options are matched by municipalities with additional contributions from industry, employers, private developers and social service agencies, depending on the target group. For example, *Edmonton’s Cornerstones Plan* has helped create 2,100 affordable rental housing units to date with a total investment of over $280 million from the Government of Alberta, non-profit organizations and private investors, leveraging $25 million. In addition to capital grants, direct subsidies could be in the form of subsidized mortgages or loans, which assist the private sector in securing additional funding (Focus, 2006). Long-term subsidies and affordable finance, aligned with appropriate level of targeting to low-income and vulnerable households, are necessary to ensure that the affordability is maintained (Berry and Hall, 2005). Interviews suggested that the subsidy programs in Alberta are very small to generate a meaningful supply of affordable rental housing. Despite a more recent resurgence in capital funding, it was clear that a much more robust and sustainable stream of direct subsidies is needed so that the private sector can secure a stable flow of additional financing through banks and credit unions. Developers indicated that it takes time to acquire such supplementary resources prior to the start of construction, which makes short-term subsidies cumbersome and often ineffective because their term expires. The need for change is also acknowledged by the provincial government (see AAHTF, 2007).

Government subsidies can also act as a deterrent to private sector involvement in affordable housing. Several private developers interviewed found government subsidies unreliable as each successive government in power tends to rescind or change the previous governments’ policies and funding requirements. Interviews indicate that subsidies generally are accompanied by complex standards and rules, which are viewed as cumbersome and add delays to a project. “Even with significant grants, the imposition of maximum rent criteria and *de facto* rent controls for 20 years has been a disincentive” (developer, interview data). Moreover, subsidies can create unfair competition between private builders by infusing money into the market for targeted projects (Ottawa Chamber, 2005).
4.3 Financial Measures

Reduction or Waiving of Municipal Fees. Municipalities use two main forms of fees to cover the administrative costs of processing a development application—permit fees and development levies—paid by developers to offset the capital costs associated with infrastructure. Municipalities typically implement development levies based on the size of the housing unit or lot being developed. The MGA allows municipalities to set their own charges and levies for development, thus allowing for reduction of fees for affordable rental housing to improve affordability (Poverty Reduction Coalition, 2006).

According to industry representatives, the municipal fees for an affordable housing project are generally nominal compared to the overall development costs. Some industry professionals stated that any reduction of those fees would be desirable because ‘every little bit counts’. However, many other for-profit developers interviewed indicated that the amount of money saved from a reduction in fees is not enough to make a significant difference. Moreover, municipalities such as the City of Calgary want to promote fairness within the development approvals process, which would result in the need to provide fee reductions for other developments providing public service (e.g. sustainable building practices or heritage preservation). Waiving or reducing municipal fees for development would not be large enough to provide significant cost savings to private developers and would require significant municipal resources to implement and manage. The marginal savings would likely not increase the supply of affordable housing.

Lending & Borrowing Practices. When direct government subsidies decrease, affordable housing developments are compelled to rely on multiple layers of financing from a variety of sources, including financial institutions (McDonald and McMiller, 2007). Financial institutions can have a significant role in making affordable housing projects more feasible by lowering the costs of debt service. CMHC can also provide lower cost access to capital for affordable housing projects under certain conditions and government guarantees (see Box 3). Some standard financing methods are:

- Lower interest rates or interest-free loans;
- Larger loans;
- Longer amortization periods;
- Reduced premium fees;
- Deferred payments; and,
- More flexible or alternative underwriting practices (Pomeroy, 2004; Myerson et al., 2007):
Box 3: Edmonton, Boardwalk 2007

Edmonton’s Cornerstone’s Initiative is a five-year plan adopted by Edmonton City Council in 2004 aimed at increasing affordable housing. All three levels of government fund the Initiative with 50% from the City of Edmonton, and 25% from both the Province of Alberta and the Government of Canada through CMHC. One aspect of this plan is to provide rent supplement for 400 rental units throughout Edmonton under the Fixed Rate Rental Supplement Pilot Project, which received $5 million in funding from the combined levels of government.

Boardwalk Rental Communities was the first private landlord to partner with the City of Edmonton’s Cornerstone’s Initiative by providing 200 units dispersed in different buildings across the city. The units are supposed to be “invisible” i.e. indistinguishable from other units in the same building. Boardwalk manages the apartments on a cost recovery basis and provides an additional subsidy of $75/unit per month if a tenant cannot afford the rent. Estimated rent level is $200 below average market rents.

Source: Interview data

Financial institutions can also contribute to the provision of affordable housing by serving as community economic developers. In Canada, credit unions and banks assume the role on a voluntary basis (Kowalchuk, 2004). For example, VanCity Credit Union created the VanCity Community Foundation that uses innovative investment policies and retention of some profits to offer loans, grants, and technical assistance for affordable housing projects. To date, there are no known financial institutions operating in this fashion in Alberta. Interviews with industry professionals indicate that the financial institutions in the province generally view lending for affordable rental housing as high risk investment. As affordable housing developments have limited opportunity to raise rents to cover budget increases, and might face community opposition in the planning process, lenders are reluctant to offer any incentives and/or more flexible underwriting standards. For borrowers, it is crucial to balance debt and equity financing to ensure cost effectiveness while also managing risk.
Philanthropy is potentially an effective method to leverage individual and corporate wealth for affordable housing projects. Donations to affordable housing projects can become a more substantial source of upfront funding in a more supportive tax environment (Manifest, 2002). Philanthropy is well established in Alberta and has already contributed to affordable rental and homeownership projects as the examples in Box 4 and 5 demonstrate. Moreover, the corporate principle of social responsibility provides a persuasive argument for contributing to socially responsible developments, such as affordable housing projects or workforce housing, which may be of particular interest in Alberta due to the importance of resource and resort industries facing labour shortages in certain areas.

Philanthropy is an effective way to engage the wider private sector beyond developers and builders in affordable housing. This method is working in Alberta, however, it does not directly benefit private developers and builders who want to build affordable housing as donations go to charitable organizations. A private builder or developer can access donations only through partnership with a non-profit organization able to fundraise.

4.4 Institutional Measures

**Housing Trusts** are a partnership of local non-profit groups, business and industry professionals, and government representatives that work together to increase and preserve affordable housing (City of Edmonton, 2007; Kowalchuk, 2004). Housing trusts are most effective if based locally, but are somewhat difficult to establish, as they require a dedicated funding source. Typically, local housing trusts rely on funding from the provincial government established through legislation, ordinance, or resolution (Manifest, 2000).

The Housing trusts are beneficial for all affordable housing developers, but especially for the private sector agents who do not necessarily want to invest time and resources to apply for government grants. A housing trust could be a primary way to provide funding for affordable housing in the most efficient way possible by channelling funds through one organization. This allows private developers the possibility of accessing a larger grant with less red tape. As many municipalities, such as Calgary, already have some form of organization that does or could function as a housing trust, the amount of resources required to implement this structure would be minimal.
Box 4: Calgary, Horizon Housing in Inglewood, 2009

The Inglewood project was developed by Horizon Housing, a not-for-profit organization dedicated to providing housing primarily for persons with mental disabilities, with $1 million from the Calgary Homeless Foundation. The 104-unit apartment building and 10 town homes were funded by a myriad of sources, both public and private, and had significant support from the City of Calgary in the form of land donation ($800,000). The units are owned and managed by Horizon Housing with tenant outreach and support provided by the Canadian Mental Health Association.

The Calgary Regional Home Builders Association provided $1 million in funding through their Foundation as well as gifts in-kind of building materials from their members. Moreover, they contributed their expertise to the design and building of the project in order to reduce costs and increase quality. Provincial funding through the Affordable Housing Partnership Initiative of over $12 million was instrumental in securing the project's viability.

Source: Interview data

Box 5: Canmore, Rundle Drive, 2008

Due to Canmore's Perpetual Affordable Housing Policy, Three Sisters Mountain Village decided to use the land they owed to develop an affordable housing complex. With help from the newly established Canmore Community Housing Association they created the necessary agreements to place restrictive covenants on the titles of each unit in order to maintain perpetual affordable homeownership of 17 of the 32 units in the townhouse complex in downtown Canmore. The cost of the market units helped subsidize the non-market units and make them more affordable. Dwellings sold for $195,900 to $289,900. Three Sisters purchased the land at full market value ($1.7 million), provided all services at no cost, contributed $2 million to the project and received no profits. The total project cost is estimated at $9.4 million.

Source: Interview data
Box 6: Housing and Land Trusts in Edmonton and Calgary

One example of a successful housing trust is the Edmonton Housing Trust Fund established in 1999. It acts as a conduit for multi-level government funds for homelessness and affordable housing initiatives. As multi-layered funding and financing is the reality in Canada, Housing Trusts can coordinate funding for affordable housing most effectively and are continually researching new sources of funding with the main goal of maintaining and creating new affordable housing opportunities. Calgary has a similar organization, the Calgary Homeless Foundation established in 1998, which provides capital funding for affordable housing projects and acts as a medium for community consultation on homelessness and affordable housing.

Calgary and Edmonton have operating land trusts. In Calgary, the Calgary Community Land Trust (CCLT) was established in 2002 and received charitable status in 2004. To date, they have provided land for three projects: Sun Court in Dover, Leo & Goldie Sheftel Court in Capitol Hill, both in partnership with Habitat for Humanity, and Kootenay Lodge in Falconridge, in partnership with the Universal Rehabilitation Service Agency.

Source: Interview data

Land Trusts are organizations that act as a steward of any land they own on behalf of the community, generally for affordable housing (Downs, 2004; Kowalchuk, 2004). Land trusts allow others to develop land for specific purposes through long-term lease agreements. They facilitate the acquisition of land as they can more easily collaborate with government in the process and are sometimes able to acquire land at a reduced cost (ibid). Land trusts are also able to receive donations of land, but the current federal tax situation acts a significant barrier to land donations for affordable housing because donations are still subject to income tax (Pomeroy, 2004). Like housing trusts, land trusts also benefit all affordable housing developers. As land is one of the most difficult barriers to overcome in building affordable housing, a land trust could significantly increase the supply by making land more available at a lower cost. Additionally, most municipalities also have organizations that are or act like land trusts.

5 Barriers for Effective Engagement: Private Sector Perspective

A small number of private developers are currently involved in building affordable housing in Alberta. Many developers and builders interviewed understand the growing need for affordable rental housing in the province and the economic and social imperatives of delivering it to the marketplace. In most of the cases
the involvement of their organization has been experimental, often associated with significant challenges. The lack of continuity illustrates that the barriers are often too difficult to overcome and that a public-private partnership model to effectively encourage private sector involvement has not been developed. These one-off projects also result in lost knowledge of how best to overcome the barriers in the process. Notwithstanding such overall sentiment, developers claim that the project has been one of their most worthwhile experiences in terms of personal satisfaction. As one interviewee states, “I’m not going to say it’s a wonderful experience, but I’m sure glad I did it, although it was hard to do” (private developer, interview data).

Private developers face a myriad of barriers to building affordable rental housing. Many are common to the entire development and homebuilding industry, but acutely affect the business practices of the private sector. These barriers consist of regulatory challenges related to the planning process and community opposition; fiscal barriers associated with senior government fiscal policy; and financial barriers, specifically obstacles related to access to loans for housing development.

5.1 Planning Barriers

Cumbersome planning approval process. According to the MGA approval of all new development projects is done on a case-by-case basis, which increases the uncertainty for the developer, as negotiations and compromise are common aspects of the process. Negotiations between municipalities and developers can extend the project timeline, as construction cannot begin until development and building permits are issued. Any increased amount of time to acquire a development permit results in increased project costs. Developers, both for-profit and non-profit, would like to see an expedited process for affordable housing applications, or at least a predictable streamlined process that reduces the amount of negotiation and compromise between city departments and developers. One developer stated, “there are abilities [sic] for the private sector to work together with municipalities and cities to create affordable housing projects—to create projects that are positive for both entities” (private developer, interview data).

Community Opposition. Another aspect of the development process that can easily increase the timeline of an affordable housing project is community opposition, or the NIMBY syndrome. The regulated procedure for public notification in Calgary is that applications are sent to the Community Association of the affected neighbourhood as well as posted on notice boards on the property and advertised in newspapers. This allows residents to comment on, or oppose, the proposed project. Developers, both for-profit and non-profit, interviewed try to engage the community from the very start of the design process to offset any
objections later due to the nature of affordable housing projects and the stigma of unsuccessful past projects. One developer experienced significant community opposition to an affordable housing project, and although the project was approved, over one year was spent altering the plans, while building costs increased. “People didn’t want to see affordable housing in their community” (private developer, interview data). If an application is rejected, the developer can either re-apply with changes that will satisfy the Development Authority or appeal the decision, which can take a considerable amount of time and add uncertainty to the project.

5.2 Fiscal Barriers

Non-existent tax incentives. The current tax environment acts as a disincentive to build affordable rental housing. Developers cannot adequately adjust rental rates to reflect increased development costs and there are no opportunities for tax deductions of capital losses. For example, a building usually takes two to three years to gain approvals, complete construction and become occupied. By that time, construction costs can increase significantly, and timelines often require extensions, which also increase the overall project cost. By the time the building is occupied, the costs can increase beyond what was initially projected. However, in an affordable rental building rents are usually set to reflect target incomes and not the project costs, which can result in a significant loss for the developer. Furthermore one limitation of tax incentives for affordable housing projects is that they do not provide upfront project funding, but instead are redeemable only once per year. Developers “use cash up front so some type of tax incentive…has to be at the beginning of the cycle when the cash is going out the door” (private developer, interview data). Thus, tax amendments alone would not be sufficient to bridge the funding gap.

Limited and complicated direct subsidies. Government grants or subsidies play a significant role in providing affordable housing, but they are seldom accessed by the private sector. Many industry professionals stated that they generally do not have the time to do the research necessary to understand the funding application guidelines or the strict timelines set to receive the funding. The result is that many for-profit developers have decided not to build affordable housing despite expressing a desire to become more involved. Since government grants or subsidies are short-term in nature, the time to apply is restricted and unless an organization keeps track of what is available on a regular basis, it is often difficult to develop a project that aligns to the funding timeframe. For those organizations that have applied for government grants, rarely is the maximum amount granted, which limits private sector participation. Thus, most private development representatives state that, based on the funding available, it is not worth applying for subsidies since the provision of affordable housing is not the primary mandate of their organ-
ization. Non-profits, on the other hand, are usually much more reliant on these subsidies because they do not have the resources to leverage funding from other sources. However, both non-profits and for-profits recognize that subsidies are generally not sufficient to close the funding gap between the development costs of the affordable housing project and the estimated revenue.

Moreover, some developers stated that the lack of clarity from senior government regarding the target groups for affordable rental housing also acts as a deterrent. In other words, there is no clear direction on what type of housing is needed and what income groups are intended to be the beneficiaries.

5.3 Financial Barriers

Restrictive Lending and Borrowing Practices. Financial institutions play a significant role in making affordable housing projects possible because they are the primary source of financing for private developers. Most private developers interviewed do not have the capital to independently finance their own projects, which forces them to rely heavily on loans. Financial institutions view affordable housing projects as high risk and so are unlikely to lend money to developers of these projects and if they do choose to provide funding, the interest rates are usually higher. Some private developers interviewed have managed to secure reasonable interest rates by relying extensively on their reputation and previous business interactions with specific financial institutions. As a result, loans for affordable housing projects are difficult to secure, which ultimately acts as another barrier to private sector involvement.

In summary, industry professionals were quite clear regarding the numerous challenges and barriers that limit private sector participation in affordable rental housing. Many private developers and builders expressed a desire to become more engaged in the process and a willingness to accept a reduced profit margin to do so, but also felt that the current environment results in a cost to developers beyond simply a reduction in profits.

6 Bridging the Gap: Recommendations for Change

Regardless of any tax credits or regulatory incentives to generate greater private sector provision of affordable housing, some form of direct subsidies is required to bridge the funding gap between the cost of development and potential revenue generation. Long-term subsidies and affordable finance are essential to generate a meaningful supply of affordable rental housing. The private sector in particular needs a much more robust and sustainable stream of direct subsidies with clear and transparent rules to become involved. Several private developers interviewed found government subsidies unreliable as each successive government in power tends to rescind or change the previous governments’ policies and funding.
requirements. Present subsidies are not only inadequate to respond to the growing need for affordable rental housing, but are accompanied by complex standards and rules, which are viewed as cumbersome and add delays to a project. Greater targeting of government subsidies to well-defined income groups along the entire housing continuum could present greater opportunities for private sector involvement.

In addition to fiscal support from senior governments, municipalities can play a significant role in facilitating private sector involvement by creating a positive planning and policy environment. Municipalities in Alberta are no longer in a position to undertake housing development directly on their own, nor can they replace what has been lost due to the withdrawal of senior governments from financial support for affordable housing. Based on analysis of literature on the topic and interviews with industry professionals, the following five recommendations constitute the most effective methods to encourage private sector participation in the provision of affordable housing. These recommendations could be implemented individually, but would be most effective if considered collectively as they are intended to compliment each other to leverage the greatest level of private sector involvement.

- **Increasing the transparency and predictability of the development approvals process.** A more streamlined process could encourage a greater willingness to pursue innovative or higher risk projects if the approval process was enhanced to become more transparent and predictable. If a developer is aware of the time required for development approvals, the associated costs could be better projected in the initial budget. While municipalities cannot guarantee development approval timelines due to unforeseen circumstances such as community opposition, a more predictable, streamlined and efficient process would reduce the constraints currently experienced by private developers of affordable housing.

- **Providing better access to land at lower costs.** In addition to land donations and provision of land at fixed price, another effective method is through long-term land leases that could provide the municipality with an asset while maintaining long-term affordability. Using a land lease model, development costs are reduced and private developers typically partner with non-profit housing organizations and/or transfer affordable rental units to municipal housing companies upon completion. Land trusts also have a critical role in assisting with the acquisition of land. In coordination with a housing trust mobilizing funds, they can act as a focal point for private sector engagement.
Introducing inclusionary zoning could allow for significant amounts of new affordable housing development. This method would also have the added benefit of creating a social mix, which is typically identified as a best practice and would facilitate community acceptance of affordable housing projects (AAHTF, 2007). The implementation could significantly affect the business practices of developers. Government funding enables applicants to utilize funds towards purchasing dedicated affordable units within market developments. The purchase of units allows private developers to pursue their standard business practice, while non-profit housing agencies could purchase units in bulk at a lower cost, thus building a portfolio of affordable housing over the long-term.

Establishing sustainable funding for affordable housing. Increasing capital funding for a continuum of affordable housing options by senior governments—federal and provincial—is essential to bridge the gap between the cost of development and potential revenue generation. The programs need to have transparent and well defined rules, standards and target groups (AAHTF, 2007). As different forms of collaboration between private, public and non-profit institutions continue to evolve, the fiscal framework, including tax incentives, needs to be adjusted to encourage more private sector engagement and buy-in. Specific instruments might be used to target a particular clientele (e.g. low-income, vulnerable and special needs households), while others might be appropriate for medium income groups that can be accommodated in near market rental and affordable homeownership housing. Capitalizing on the competitive advantages of the private sector (promote/finance, design/build) to reduce development costs through innovative construction and/or management efficiencies should be promoted (CBC, 2010).

Enhancing the role of philanthropy. Increased awareness of the challenges associated with developing affordable housing would encourage greater private sector contribution of funds for specific projects. Time and expertise contributed by the development and homebuilding industry to assist with affordable housing projects can significantly contribute to increasing the supply of affordable housing. The experimental nature of affordable rental project so far demonstrates the potential of effective partnerships or collaborative relationships with municipalities and non-profit housing providers.
Acknowledgements
The authors acknowledge the financial support of the United Way and Calgary Real Estate Foundation through grant-in-aid of research administered by Cities, Policy & Planning lab at the University of Calgary.

Notes
1 Approximately 35,000 Calgary families have affordability problems as housing prices have increased 156% over the past ten years, while incomes have increased by 34% (Calgary Committee to End Homelessness 2008). Fort McMurray has some of the highest rents and housing prices in Canada as a result of a “boomtown” phenomenon of rapid population growth (over 50%) and a housing deficit of 2,840 dwellings (Stubbs et al., 2007).
2 For example, total funding for 2010/2011 program is $188.3 million, $38 million of which is federal funding. This is allocated to 27 projects developing 1,080 housing units for low-to-moderate income Albertans, individuals with special needs and homeless people (Interview data 2011).
3 “The City’s approach is to force the developer to include units as a condition of approval. This isn’t very fair, but perhaps trades could be made in the amount of open space provided or some requirements for infrastructure improvements” (development consultant, interview data).
4 The City of Vancouver is the leading example of a Canadian municipality that has utilized an inclusionary zoning policy requiring major developments to include 20 percent social housing since 1988. The City of Edmonton has experimented with inclusionary zoning in its inner city initiatives and projects that amendments to the Municipal Government Act in that regard would enable the development of 400 affordable housing units annually (City of Edmonton 2007).
5 Cyprus Greens (CFB West) has 65 single family dwellings for low-income families operated and owned by the municipal housing company. The rental housing was developed with $4.7 million City contribution, donation of land by Canada Lands and contribution by a private developer refurbishing the units at cost.
6 The Cornerstones Plan aims to create 2,500 affordable housing units by the end of 2011. Its most recent project Baranow Estates is built and owned by Giacobbo Holdings Ltd. The new $6.1 million four-storey building has 51 rental apartments with rents that do not exceed 85% of average market rents for 20 years (Interview data 2011).
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