THE CITY OF
CALGARY
CITY AUDITOR'S OFFICE

Attainable Homes Acquisition and Development Cycle Audit

April 6, 2016

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Executive Summary

Attainable Homes Calgary Corporation (AHCC) is a not for profit subsidiary of The City of Calgary, created to address the housing affordability gap. Our audit objective was to provide assurance on the effectiveness of acquisition and development cycle processes, which support the mandate of AHCC. These processes support AHCC's mandate by providing quality homes at affordable prices and ensuring discounted land, obtained from The City, is appropriately leveraged. The City sold eight sites to AHCC at book value of $6 million, an $11 million discount on market value at the time of sale.

AHCC acquire inventory (apartment condos and townhomes) through land developments and unit acquisitions. In a land development AHCC provide land to a developer and in return receive future units priced below market and payment for the land. Unit acquisitions are bulk purchases of units from a developer's existing or planned development. Our audit evaluated controls that supported unit acquisitions and land development contracts signed from October 1, 2014 to September 30, 2015. Under these contracts AHCC acquired 185 units to support their program.

Acquisition and development processes were effective in supporting acquisition of units for the program during the audit period under review. However, controls in place were not sufficient to mitigate risk in partner selection for land developments and ensure the long term financial sustainability of the subsidiary.

We assessed controls in place to mitigate risk in the land development process of conflict of interest in developer selection, partnering with a developer that does not provide optimum value, and/or has insufficient financial capacity to complete a project. Competitive procurement processes mitigate many of these risks as they are open and transparent and provide a range of development options. Although AHCC has established procurement and conflict of interest policies, these policies do not provide sufficient direction to management to mitigate land development risks. We noted policies do not establish when competitive procurement should be followed or clearly define a process for disclosing conflicts of interest. Non-competitive processes established by management for selecting two land development partners during our audit (referred to by AHCC as "prequalified") did not include documented selection criteria or a process for including new partners. In addition, a defined process did not exist to evaluate the financial capacity of development partners.

Management provides reporting to the Board to allow them to evaluate a given land development or unit acquisition prior to giving approval. These reports provide relevant information on the qualitative aspects of a transaction such as location and proposed design. However, reports do not include sufficient information to evaluate return on investment. Unit acquisition information does not include a consistently calculated margin. Land development transactions have greater complexity and should include a pro forma budget capturing land sale proceeds, revenue from unit sales, costs to purchase the units and any financing costs.

In total, 12 recommendations are included in Section 4, which should not require additional resources to implement. Management agreed with the recommendations and have committed to implement action plans by September 30, 2016.

1.0 Background

Attainable Homes Calgary Corporation (AHCC) is a non-profit organization and a wholly owned subsidiary of The City of Calgary (The City) created to address the housing affordability gap. AHCC was incorporated in 2009 and is governed by a Board of Directors, who report to City Council.

AHCC's mandate is "Creating value-driven developments using innovative financing solutions with our partners and communities underpins our success in providing quality entry-level homes at attainable prices". The mandate is achieved by partnering with builders and developers and negotiating discounts that allow AHCC to sell homes to qualifying buyers at below market prices.

AHCC acquires apartment condo and townhome units through two methods. First, units in land development projects are sourced by leveraging eight land sites acquired from The City, at their book value (historical cost) of $6 million, representing an $11 million discount on market value of $17 million. In these projects AHCC provides the land to construction projects, secured by an interest free vendor take back mortgage, in return for housing units and payment of the market price of land, upon completion. Variations within this method that AHHC has pursued include participating as a joint venture partner and contributing an additional interest free loan.

Second, AHCC sources units in acquisition projects by bulk purchasing units from builders in existing developments, where suitable pricing discounts can be negotiated. Benefits to developers of bulk purchases include potentially generating presales for construction financing and savings on marketing costs.

AHCC enables eligible participants to purchase a home at below market price by providing a forgivable equity loan (non-cash down payment). In return buyers contribute a $2,000 deposit and, upon resale or refinancing, share their property appreciation with AHCC (shared equity model). To offer this program AHCC purchases units at approximately a 9% -12% discount on market value. This allows the discount on market price to the buyer, the non-cash down payment, and a profit margin for AHCC. The profit margin covers AHCC's overhead expenses, which are approximately $2 million per year. AHCC has targeted sales of approximately 175 – 225 units per year to cover overhead expenses and ensure sustainability of the shared equity model.

An audit of the AHCC acquisition and development cycle was included in the City Auditor's 2015 Annual Audit Plan for two reasons. First, processes within this cycle have a significant impact on AHCC's ability to provide quality homes at attainable prices and achieve business objectives. Second, the discount provided on land sold to AHCC is significant and should be appropriately leveraged to achieve value for The City.

2.0 Audit Objectives, Scope and Approach

2.1 Audit Objective

The objective of this risk-based audit was to provide assurance on the effectiveness of acquisition and development cycle processes that support the mandate of AHCC. The objective was achieved by assessing the design and effectiveness of controls in place to mitigate the following eight risks:

1. Partnering with developers that lack the financial capacity to complete the project or produce low quality units;
2. Conflict of interest in developer selection;
3. Pricing of units sourced does not allow for a sufficient margin when considering the selling price to program participants;
4. AHCC has excess inventory due to an inability to secure buyers;
5. Insufficient units are sourced;
6. Contracts do not mitigate AHCC's liability in situations where developers do not adequately perform their duties;
7. Development deals where AHCC contributes land do not achieve a sufficient return on investment; and
8. AHCC sell homes at a loss or take ownership of properties due to decline in Calgary property prices between the time of entering into firm commitment and subsequent sale to homebuyers.

2.2 Audit Scope

Our audit evaluated controls that supported unit acquisitions and land development contracts signed from October 1, 2014 to September 30, 2015. Contracts included two land development projects (one involved two separate sites and contracts[1]) and four unit acquisition projects for bulk purchases. Controls that did not relate to specific transactions, were tested based upon performance during the same period.

Assessment of the long term sustainability of the AHCC shared equity model was out of scope. AHCC in their 2015 risk register indicated that KPMG conducted stress testing on AHCC's five year business plan.

2.3 Audit Approach

Our audit approach included conducting interviews with management to understand processes and testing the controls identified in the Risk Assessment in Appendix A.

[1] AHCC signed two linked contracts for this development. Both land and interest free financing were provided through this agreement. Units were contracted on land previously owned by AHCC and another site owned by the developer.

3.0 Results

The acquisition and development cycle consists of partner selection, contract development, board approval and ongoing monitoring. At each stage of the cycle we evaluated the effectiveness of controls in mitigating the risks outlined in section 2.1 for all contracts included in the audit scope. We raised 12 recommendations to improve the design and operating effectiveness of controls over the cycle. In addition, we verbally provided management recommendations for efficiency improvements.

Partner Selection
Unit acquisition partner selection controls were appropriate given their lower risk exposure. These transactions involve the purchase or option to purchase units in a developer's existing or planned development and are less complex. Furthermore, AHCC capital tied up in these transactions is normally[2] limited to the unit deposit.

Land development partner selection controls were insufficient. AHCC developed board approved policies for procurement, conflict of interest and delegation of authority. However, these policies did not provide adequate direction to management to mitigate the risks of conflict of interest, failing to achieve value for money and ensuring the developer had the financial capacity to complete the project.

Contract Development
Controls that protected AHCC's interest in land and mitigated legal liability in the contract development stage were effective. All contracts were reviewed by legal counsel, mitigating AHCC's liability in situations where developers do not adequately perform their duties.

Land contributed to development projects was protected by a vendor take back mortgage for the appraised value, which was recorded on the land title. Vendor take back mortgages are subordinate to the developer's construction financing. In addition, AHCC had considered the risk associated with construction financing on land development projects and the Development Manager was reviewing and approving financing terms. We encouraged management to reflect their effective process in formalized policy.

Board Approval
Processes exist to seek board approval for land development and unit acquisition transactions. Board approval is a control that ensures that projects are consistent with AHCC's goals and objectives and provide sufficient return on investment. We reviewed all projects presented to the Board during the audit period and noted that AHCC did not seek board approval for one project prior to signing the contract. Approval for this transaction, which was for the purchase of eight townhomes, was obtained at a subsequent board meeting.

Board reports produced by management addressed the non-financial considerations of site design, location desirability and client pricing. However, board reports did not provide sufficient information for the Board to evaluate return on investment.

[2] In the case of a firm purchase agreement, AHCC may have to take possession of unsold units, which increases the capital tied up from the deposit to the full purchase price.

Information required to assess return on investment varies between unit acquisitions and land developments. Information needed for a unit acquisition transaction is a consistently calculated margin. A land development is a more complicated transaction that requires a pro forma budget capturing land sale proceeds, revenue from unit sales, costs to purchase the units and any financing costs. Return on investment for land development projects needs to be considered holistically as a greater margin on the sale of units could be achieved as a result of AHCC agreeing to a lower price on the land.

Ongoing Monitoring

Ongoing monitoring consists of management's monitoring of individual projects and board oversight. Effective processes existed to track land development projects against schedule. Key performance indicators were provided to the Board on a monthly basis, which support monitoring of margins and the supply of inventory.

In July 2015, management initiated additional reporting to the Board through a market conditions report. We identified an improvement opportunity to tie market conditions to the impact on AHCC's current inventory and future commitments. This improvement will provide information to the Board on management's strategies to manage declines in Calgary property prices and the impact should AHCC need to take ownership of properties or sell them at a loss.

4.0 Observations and Recommendations

4.1 Financial Analysis of Transactions

Reports provided to the Board seeking approval of four unit acquisitions and two land development transactions focused on qualitative criteria and did not include sufficient information to evaluate the return on investment. Board reports should include both quantitative and qualitative criteria to support decisions that achieve optimal value for the organization. Achieving a sufficient return on each transaction contributes to ensuring the long term financial sustainability of AHCC as an organization that can continue delivering homes without requiring ongoing external financial support.

The Development Manager prepares reports for proposed land development and unit acquisition projects, which are presented to the Board for their approval. We reviewed the reports submitted to the Board for the two land development and four unit acquisition contracts signed during the audit period under review.

The land development reports for the land development projects contained information on the type of units acquired, total number of units in the project and the proposed developer. Although commentary on pricing ranges and the approximate gain on sale of land was also included in the report, specific values were not stated. As a result, the reports do not include sufficient information for the Board to evaluate return on investment. Proper analysis would require a pro forma budget that captures the expected profit from the sale of land and expected margins on the sale of units including purchase costs and any soft costs incurred by AHCC (e.g. consultant fees and permitting). Financing costs such as interest free equity financing should also be included.

Additional disclosure is needed to properly evaluate the sale price of the land. AHCC is expected to receive market value for land contributed to these transactions. However, market value is subjective and varies based upon comparables used in calculating the appraised amount. The final price is a negotiated amount between appraisals conducted by the developer and AHCC. In one development project the price received for land was negotiated down by $200,000 after board approval and original contract execution because of the difference between appraisals. The amended contract was not signed by the Chair of the Board.

Unit acquisition reports provide information on the type of units, market pricing, location and discount offered to AHCC. However, pricing and discount information is not sufficient to determine the profit margin to AHCC and directly calculate return on investment. First, AHCC cannot always take advantage of the full discount due to its selling price cap of $329,900, including net GST ($319,671 excluding GST). Second, AHCC provides an additional discount below the market price or price ceiling, which further impacts the margin.

Unit acquisition reports reviewed presented pricing and discount information on a different basis. For example, one report included discount information using figures that included GST, whereas another was presented excluding GST.

Finally, unit acquisition reports did not indicate when there was uncertainty around selling price. This occurs in situations where mortgage insurer approval was not achieved for all units at the time of the board report. An example is one unit acquisition, where Genworth approval was achieved for 31% of the units at the time of the board report and contract signing. To insure that balance with Canada Home Mortgage Corporation, AHCC was required to discount the selling price.

Although the concept of optimal value is part of both the Development Policy and the Financial Policy & Authorities Policy, there is no specific guidance for assessing return on investment, and determining optimal value. Reports to the Board reflect this lack of guidance.

<u>Recommendation 1</u>
AHCC's President and CEO ensure that land development and unit acquisition board reports incorporate return on investment analysis, and determine when changes to expected returns require board notification.

The board reports should be prepared using standard templates for both unit acquisition and land development projects that incorporate the following:

1. For unit acquisition transactions, include information on expected margins (price paid by customer excluding GST - price paid by AHCC to builder excluding GST), expressed both as a total dollar amount and as a percentage of the sales price.
2. For land transactions include:
   - Pro forma budgets that capture revenue from the selling price of land and units, and costs to purchase the units, including financing costs and any soft costs borne by AHCC; and
   - All appraised values for the land and comparables used to arrive at the land value.

<u>Management Response</u>

Agree.

Action Plan	Responsibility
AHCC will develop a standardized ROI formula for each transaction type and include this on board reports. The board reports will also be standardized to include non-financial attributes desired by AHCC's mandate.	Lead: Development Manager Support: Financial Manager, AHCC, CEO and Board Commitment Date: September 30, 2016

4.2 Procurement Policy

When delivering land development projects, AHCC's procurement policy does not define when a competitive procurement process should be followed, such as when a tender process through a Request for Proposal (RFP) is appropriate. Clearly defining procurement expectations ensures that an open and transparent procurement process is consistently followed, which mitigates the risk that there is conflict of interest in developer selection and the risk that optimal value for money will not be achieved.

Procurement policy, is defined in AHCC's Financial Policy & Authorities Policy. The overall procurement objective in Section 2.1 of the policy includes ensuring optimal value for money and that a transparent, fair and objective process of selection is utilized. The document states under Section 2.2 (Principles) that AHCC's practices will follow accepted standard municipal standards and practices and will be guided by principles that include: Be equitable and transparent; and Use a competitive process wherever appropriate. Section 2.5 (Competitive Process) states "Where appropriate, a tender process will be initiated through a Request for Proposal (RFP)".

The policy does not define when a competitive RFP process is appropriate or when it is acceptable to use a prequalified vendor (See prequalified observation below). In 2012 and 2013 AHCC initiated RFPs to solicit tenders for the development of two sites. The developers that were shortlisted became part of a pre-qualified list. Land developments awarded during our audit period were selected from this pre-qualified list following a non-competitive process. The policy has not been updated to reflect when awards can be made by selecting from a pre-qualified list versus a competitive process.

Recommendation 2

AHCC's President and CEO determine threshold conditions when a competitive (RFP) process should be followed and when a non-competitive prequalified process is acceptable and update the Financial Policy & Authorities Policy accordingly.

Management Response

Agree.

Action Plan	Responsibility
AHCC will develop a procurement policy that addresses items 4.2, 4.3 & 4.4 in this report. The policy will include thresholds and conditions for projects where a non-competitive process may be acceptable.	Lead: Development Manager Support: CEO, AHCC Commitment Date: September 30, 2016

4.3 Prequalified Process

AHCC has not defined and documented the criteria to select partners for land development contracts from the pre-qualified list (sole source) or add partners to the pre-qualified list. Without criteria for the selection of partners through sole sourcing, processes may not support achieving optimal value and transparency in the awarding of contracts to mitigate the risk of conflicts of interest.

Both land development contracts awarded during the audit period were awarded by selecting the developers from a pre-qualified list. Management advised that inclusion on the list is based upon performance in previous RFPs. We confirmed that developers selected from this list during the audit period were successful proponents in a previous RFP. The last opportunity to be included on this prequalified listing was an RFP that closed prior to the audit period under review.

Management advised that a decision is made between the CEO and management on which developer is the most appropriate for a given project. Factors considered include the expertise of the developer in building the type of units (e.g. townhomes) and ensuring too much work is not concentrated with a single partner. This decision is then recommended to the Board for approval. However, no formal selection criteria support this decision other than those implied in previous RFPs.

AHCC's Financial Policy & Authorities Policy provides guidance on sole sourcing in Section 2.6 and states: "From time to time, AHCC may elect to approach a particular builder or developer to prepare a proposal for development. AHCC may have experience with the proponent and the proponent may be perceived as in a unique position to provide a desired development. When sole sourcing, all arrangements must be well documented." The sole sourcing policy does not require that the selected proponent have experience with AHCC and/or be the only developer that can provide a desired development. There is no specific guidance that defines the current process for awarding contracts to existing pre-qualified developers.

Recommendation 3

AHCC's President and CEO develop, document and implement a process to allow the inclusion of new partners on the pre-qualified list for land developments and remove existing partners as appropriate. This process should include public advertisement of the opportunity (e.g. through AHCC website and defined criteria for inclusion or removal).

Management Response

Agree.

Action Plan	**Responsibility**
AHCC will develop a procurement policy that addresses items 4.2, 4.3 & 4.4 in this report. This policy will include a process to allow the inclusion of new partners on the pre-qualified list for land developments and remove existing partners as appropriate. This process will include public advertising of the opportunity through the AHCC website and defined criteria for inclusion or removal.	Lead: Development Manager Support: CEO, AHCC Commitment Date: September 30, 2016

Recommendation 4

AHCC's President and CEO determine the criteria that must be met to select developers from the pre-qualified list (sole source) for land development projects including the retention of documentation supporting the selection and how this information will be summarized when bringing the decision to the Board for approval.

Management Response

Agree.

Action Plan	Responsibility
As part of the procurement policy, AHCC will develop a process for selecting or short-listing partners from the pre-qualified list.	Lead: Development Manager Support: CEO, AHCC, Board Commitment Date: September 30, 2016

4.4 Financial Evaluations

There is no defined process to evaluate the financial capacity of potential land development partners at the time of the initial RFP or to reassess prior to any subsequent award through the pre-qualified process. The process to evaluate financial capacity of potential developers should be documented to assess their ability to complete the project. In a land development project, AHCC sells the land to the developer and is protected by a vendor take back mortgage that is subordinate to bank construction financing. If the developer is financially unable to complete the project the land could be repossessed by the bank, which could lead to delays in the project and legal costs, when AHCC seeks to regain possession of the land.

During the audit period, land development contracts were signed with two developers. As noted above, both developers were successful proponents in a previous award through a RFP. Respondents to a RFP are required to submit financial information to be scored against the RFP criteria. No evidence of a specific financial evaluation by AHCC from the RFP was available for either developer. Although the developers partnered with AHCC on previous projects, no formal updated evaluation was performed when the subsequent awards were made.

AHCC advised that some RFP respondents were unwilling to provide financial statements due to the privately held nature of the company or were new companies with no prior history. Although there has been staff turnover since the RFPs were conducted, AHCC confirmed that currently there is no defined process to evaluate the financial capacity of developers that respond to a RFP or that are selected from the pre-qualified list. In addition, there are no alternate means to evaluate where financial information is not readily available.

Recommendation 5

AHCC's President and CEO define and document the process to evaluate the financial capacity of prospective land development partners, which includes alternate means for evaluating partners when financial information is not readily available. The process should include evaluation for procurement through a Request for Proposal or selection from the pre-qualified list.

Management Response

Agree.

Action Plan	Responsibility
AHCC will develop a procurement policy that addresses items 4.2, 4.3 & 4.4 in this report. This will include an analysis of the financial capacity of prospective partners, including alternate means for evaluating partners when financial information is not readily available.	Lead: Development Manager Support: CEO, Financial Manager, Board Commitment Date: September 30, 2016

4.5 Conflict of Interest Disclosure

Although an employee conflict of interest was disclosed to the former President and CEO and former Chair of the Board, it was not disclosed to the entire Board in accordance with the AHCC Conflict of Interest Policy. Conflicts of interest should be disclosed to the Board to provide information to properly evaluate the conflict and the proposed action and mitigate the risk of significant reputational damage. Reputational damage can arise through both actual and perceived conflicts of interest.

The conflict was disclosed to the President and CEO of AHCC and the Board chair. However, the President and CEO did not disclose the conflict at the next Board of Directors meeting in accordance with section 4(F) of the AHCC Conflict of Interest Policy that states "The Chair or President and CEO may rule on the conflict and may either require the termination of the activity or consent to it in writing. Any such decisions must be disclosed at the next meeting of the Board of Directors."

AHCC's Conflict of Interest Policy is not clear. For example, the policy's use of language such as "a direct or indirect pecuniary interest" and the definition of a conflict of interest, where in one part it refers to a "close relative" and in another section "any relative".

Recommendation 6

AHCC's President and CEO disclose the employee conflict of interest at the next board meeting and ensure that the disclosure is recorded in the meeting minutes.

Management Response

Agree.

Action Plan	Responsibility
The employee conflict of interest to be disclosed at the next available board meeting, and recorded in the meeting minutes.	Lead: CEO Support: Board Commitment Date: Actioned March 9, 2016

Recommendation 7
AHCC's President and CEO require annual disclosure of conflicts of interest to the Board and immediate disclosure when a conflict of interest relates to a transaction presented to the Board. AHCC's Conflict of Interest Policy should be updated accordingly, including clarification of language.

Management Response

Agree.

Action Plan	Responsibility
AHCC will require annual disclosure of conflicts of interest to the Board and immediate disclosure when a conflict of interest relates to a transaction presented to the Board. AHCC's Conflict of Interest Policy to be updated accordingly, including clarification of language.	Lead: CEO, AHCC, Financial Manager Support: Corporate Performance & Governance Committee Commitment Date: September 30, 2016

4.6 Board Approval

One out of the seven unit acquisition/development contracts signed during the audit period was not approved by the Board prior to execution. All unit acquisitions should be approved by the Board as outlined in Section 3.4 of AHCC's Financial Policy & Authorities Policy. In the absence of board approval or other delegated authority, there is a risk that AHCC may enter into agreements that have not been properly evaluated.

We reviewed all unit acquisition contracts signed during the audit period. Section 3.4 of the AHCC Financial Policy & Authorities Policy states that "The Board of Directors will have final authority on all purchase and sale of land, property and leasehold arrangements". One contract was signed on December 1, 2014 prior to board approval on December 11, 2014. The project was for the purchase of eight town homes.

Management advised that this agreement was signed prior to board approval since the acquisition was with an existing developer and there was time sensitivity to reach agreement without waiting for the next board meeting. To allow board approval without delay, as of June 25, 2015, AHCC subsequently implemented Policy #13- Board Meetings that provides for meetings to be transacted by email poll or teleconference to vote on a specific item or items. Email votes must have unanimous board consent.

Recommendation 8

AHCC President and CEO ensure that board approval is received prior to contract execution.

Management Response

Agree.

Action Plan	Responsibility
Management will ensure that contracts are approved by the Board prior to execution. Policy #13 – Board Meetings has been amended to allow email votes. Email approval will be sought in cases when timing prevents waiting for a regular board meeting to seek approval.	Lead: AHCC President and CEO Support: N/A Commitment Date: April 1, 2016

4.7 Construction Financing Delegated Authority

The Development Manager's role in approving construction financing is not formally documented in AHCC's Financial Policy and Authorities Policy. Authority to approve construction financing should be documented in a board approved policy. Failure to document this role and authority in policy may create ambiguity in responsibility for this task and with organizational turnover may result in this key task being performed inconsistently.

Land AHCC provides to a development project is secured by an AHCC vendor take back mortgage, which is subordinated to construction financing arranged by the developer. One of the two land development contracts signed during the audit period under review included a condition precedent that AHCC approve the construction financing for the project.

The AHCC Development Manager reviews and approves this construction financing to protect the interests of AHCC. The approval of construction financing is key since the Development Manager checks to ensure that financing is specific to the AHCC project and reflects market interest rates. These help mitigate the risk that land is repossessed by the bank due to the developer's inability to make payments as a result of a high interest rate or problems on another development. The construction financing on two pieces of land transferred during the audit period were reviewed by the Development Manager. Although the Development Manager approved the construction financing as outlined in one of the contracts, the authority to approve has not been delegated to the Development Manager and is not included in the Financial Policy and Authorities Policy.

The lack of documentation around this approval authority reflects that section 1.2 of the policy considers the initial land contract but does not consider the subsequent construction financing approval embedded in the contracts.

Recommendation 9
AHCC's President and CEO update the Financial Policy and Authorities Policy to reflect the Development Manager's approval authorities for construction financing on land transferred to development projects.

Management Response

Agree.

Action Plan	Responsibility
AHCC to update the Financial Policy and Authorities Policy to include approval authorities for construction financing review where required. Management will obtain board approval for this policy change.	Lead: CEO, AHCC, Financial Manager Support: Audit & Accountability Committee Commitment Date: September 30, 2016

4.8 Market Conditions Report

The current market conditions report to the Board provides general commentary, which is not specific to AHCC's current inventory and future commitments. The Board should have information that specifically relates changes in the market to AHCC's ability to sell and acquire units, along with proposed management actions where concerns are identified. If the organization does not react to changes in market conditions it may sell excess inventory at a loss or take ownership of properties.

A report was presented to the Board on June 25, 2015, analyzing current market conditions. This report provided a high level overview of the market and a solution for AHCC to react to changes in the market through agreements that combine firm sales, along with an option to purchase additional units. The report was generic and did not provide analysis of changes in the market and impact on current and future inventory projects, including what impact these changes would have on prices and margins. Without this information, the Board may not be aware of concerns that require management action.

This was the first market conditions report to the Board. As a result, no criteria were outlined for types of information the Board requires in these reports.

Recommendation 10

AHCC's Development Manager, in consultation with the Board, develop reporting that allows the Board to assess the impact of market conditions on current and committed inventory.

Management Response

Agree.

Action Plan	Responsibility
Management believes the Board's independent expertise and recommendations regarding market conditions should be utilized. The AHCC Board comprises industry leaders who contribute their expertise and guidance on market conditions. AHCC's Development Manager will work with the Board to develop a way to track committed inventory against changes in market conditions. This may become part of the existing monthly KPI document.	Lead: Development Manager Support: Sales Manager, Financial Manager, Board Commitment Date: September 30, 2016

4.9 Mortgage Affordability Calculator/Price Ceiling

The assumptions, the price ceiling calculation is based on, are outdated and there is no process to update the calculation. Price ceiling calculations should be updated periodically to reflect changes in program criteria and changes in home ownership costs. This calculation provides key information on the maximum selling price that the majority of program participants can afford, which impacts the cost and type of units AHCC can acquire and margins to cover overhead expenses.

AHCC calculates the maximum price ceiling that units can be sold for using the following criteria: property tax; condo fees; other debt payments; a 25 year amortization period (consistent with Canada Mortgage Housing Company rules); and interest rates that are reflective of the market. AHCC has not updated the ceiling price calculation in the last four years and, as a result, assumptions for home ownership expenses for debt, property taxes and condo fees are outdated. Also, AHCC program changes regarding forgivable down payment loans and maximum household income were not reflected.

Recommendation 11

AHCC's Sales and Marketing Manager annually review the assumptions that form the basis of the price ceiling calculation and update accordingly to reflect:

- Current AHCC income thresholds;
- Current forgivable down payment loans; and
- Changes in home ownership costs.

Changes to ceiling price should be communicated to the Board.

Management Response

Agree.

Action Plan	Responsibility
AHCC will develop a template for the price ceiling calculation and will include consideration of: • AHCC income thresholds • Current interest rates • Avg. Calgary debt levels • Reported client income levels Changes to the ceiling price will be communicated to the Board.	Lead: CEO Support: Development Manager, Financial Manager, Sales Manager, Board Commitment Date: September 30, 2016

4.10 Below market discounts

AHCC provided an additional price discount on units where an embedded discount to their $329,900 price ceiling was already included. AHCC should only provide price discounts to meet mortgage insurance standards (1% below market), maintain relative sales values, and for reasons that clearly support the organization's mandate. Additional, discounts result in lost revenue that cannot be reinvested in the program and cover overhead expenses.

Additional price discounts were provided for one project, which was one of the six developments tested. This development had three bedroom units that were appraised above the price ceiling. An additional 1% discount, below the price ceiling, was given for end units and 2.5% was given for interior units and result in potential lost revenue.

These additional discounts were a result of applying a 1% discount mechanically in pricing spreadsheets.

Recommendation 12

AHCC's Development Manager ensure that additional price discounts are not offered below the ceiling price, except to maintain relative values within a building or to meet the organization's mandate.

Management Response

Agree.

Action Plan	**Responsibility**
AHCC's Development Manager to ensure that additional price discounts are not offered below the ceiling price, except to maintain relative values within a building or otherwise deemed appropriate by the President and CEO. Standardized pricing template to be revised to ensure it does not mechanically reduce the price of units with values above the price ceiling.	Lead: Development Manager Support: Financial Manager, Development Coordinator Commitment Date: April 30, 2016

Appendix A- Risk Assessment

#	Risk	Description of Risk Impact	Risk Before Controls	Controls in place
1	Partnering with developers that lack the financial capacity to complete the project or produce low quality units.	Damage to AHCC's reputation, project delays and financial losses.	H	C1 - For each development, developers are selected from either a prequalified list or a formal Request for Proposal (RFP) that includes an evaluation of the financial capacity of the firm.
				C2 - AHCC Board approves both land developments and unit acquisitions based upon a report prepared by the Development Manager.
				C3 - For each development project, the terms of construction financing are approved by AHCC
				C4 - For each development, the Development Manager reviews the unit specifications and has an appraisal conducted that compares the unit's price and specifications to other comparables.
				C5 - The Development Manager reviews progress reports to track project status.
2	Conflict of interest in developer selection	Damage to AHCC's reputation and non-compliance with the New West Partnership Trade Agreement (NWPTA).	H	C1 - For each development, developers are selected from either a prequalified list or a RFP that includes an evaluation of the financial capacity of the firm.
3	Pricing of units sourced does not allow for a sufficient margin when considering the selling price to program participants.	AHCC is unable to cover its overhead and as a consequence the organization is not sustainable.	H	C6 - AHCC calculates a maximum ceiling price a unit can be sold for based upon income of program participants.

#	Risk	Description of Risk Impact	Risk Before Controls	Controls in place
				C7 - For each development or unit acquisition pricing spreadsheets are completed to determine the selling price of units based upon their cost and required margin. Market pricing is supported by an appraisal and / or underwriter approval. Pricing documentation is reviewed by the Finance Manager as evidenced by initials and date.
				C8 - On a monthly basis the Finance Manager prepares monthly KPIs for the Board that capture gross margin on sale of units, number of units sold, units possessions, number of months inventory supply and operating expense coverage (margin on sales / operating expenses for the period).
				C2 - AHCC Board approves both land developments and unit acquisitions based upon a report prepared by the Development Manager.
4	AHCC has excess inventory due to an inability to secure buyers	AHCC does not generate sufficient revenue to cover its overheads, which is identified in its 2015 business plan as between 175 - 225 units per year. Working capital is tied up in inventory.	H	C2 - AHCC Board approves both land developments and unit acquisitions based upon a report prepared by the Development Manager.
				C9 -The Development Manager monitors market conditions and presents quarterly reports to the Board. The Development Manager mitigates this risk through negotiations on fewer number of units acquired, longer timeframe to sell and discounts on market price.

#	Risk	Description of Risk Impact	Risk Before Controls	Controls in place
5	Insufficient units are sourced.	AHCC does not generate sufficient revenue to cover its overheads, which is identified in its 2015 business plan as between 175 - 225 units per year.	H	C10 - On a weekly basis, the management team reviews pipeline reporting.
				C8 - On a monthly basis the Finance Manager prepares monthly KPIs for the Board that capture gross margin on sale of units, number of units sold, units possessions, number of months inventory supply and operating expense coverage (margin on sales / operating expenses for the period).
				C5 - The Development Manager reviews progress reports to track project status.
6	Contracts do not mitigate AHCC's liability in situations where developers do not adequately perform their duties.	Delays to projects and financial losses from lawsuits	H	C11 - Legal counsel review changes to the standard agreement arising from the Development Manager's negotiations with developers.
7	Development deals where AHCC contributes land do not achieve a sufficient return on investment.	AHCC does not leverage the land to get the best deal in terms of units. Insufficient funds to reinvest back in program to cover overheads and for future expansion. Dissatisfaction from council due to the failure of the program to meet its objectives.	H	C1 - For each development, developers are selected from either a prequalified list or a RFP that includes an evaluation of the financial capacity of the firm.
				C12 - Each land piece contributed to a development project is appraised and secured by a vendor take back mortgage reflecting the market value in the appraisal.
				C2 - AHCC Board approves both land developments and unit acquisitions based upon a report prepared by the Development Manager.

#	Risk	Description of Risk Impact	Risk Before Controls	Controls in place
8	AHCC sell homes at a loss or take ownership of properties due to decline in Calgary property prices between the time of entering into firm commitment and subsequent sale to homebuyers.	Loss of income to cover overheads or reinvest in the program. Damage to AHCC's reputation.	H	C9 -The Development Manager monitors market conditions and presents quarterly reports to the Board. The Development Manager mitigates this risk through negotiations on fewer number of units acquired, longer timeframe to sell and discounts on market price.