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Subject: Report – Hudson Mews Complaints

Introduction

On December 11, 2009, the Office of the Comptroller General (OCG) received a complaint about the proposed sale of the former Hudson Bay (the Bay) property located in downtown Victoria to the BC Housing Management Commission (BC Housing). Specifically, the complainant alleged that the Hudson Mews project was receiving a 'bail out' from the provincial government due to the influence of a former Cabinet Minister who is related to the owner of the Bay property. This allegation, if proven, would constitute a non-arms-length transaction, putting BC Housing in a conflict of interest.

In addition, the OCG received a separate complaint from the ^{15(1)(d)} expressed their concerns involving the public tendering process respecting construction of the Hudson Mews project on the former Bay property. Specifically, the ^{15(1)(d)} was concerned that the company that was direct awarded a contract to manage the Hudson Mews project (TL Housing Solutions Ltd.) would not follow public sector procurement policies that require a public tendering process to hire subcontractors.

The OCG received both of these complaints following the Ministry of Housing and Social Development's (the ministry) December 7, 2009, public announcement of the \$32.8 million Hudson Mews project.

The Comptroller General promptly requested that Internal Audit & Advisory Services (IAAS) look into both complaints.

Background

BC Housing is a provincial crown agency under the ministry. BC Housing's mandate is to fulfill the province's development, management, and administration of subsidized housing as set out in the Shareholder's Letter of Expectations.

Guided by Housing Matters BC, the provincial housing strategy, BC Housing invests in housing and shelter programs to ensure British Columbians have affordable and appropriate housing.

BC Housing ensures social housing is well managed and well maintained over the long term. BC Housing also provides financial, administrative, and technical support to non-profit and co-op housing providers, and oversight through long-term operating agreements.

The ministry's December 7, 2009, public announcement indicated that the Hudson Mews would provide 120 units consisting of affordable rental units, affordable home-ownership units and commercial space. On the same day, BC Housing issued an expression of interest (EOI) seeking a non-profit society to own and operate the Hudson Mews. The EOI described the Hudson Mews as a development to provide housing for low to moderate household incomes (i.e. household pre-tax incomes that do not exceed \$57,977).

Timeline of Key Events

- In early 2005, S-8129 Holdings Ltd., a company related to the Townline Group of Companies acquired the former Hudson Bay property for a reported \$15.5 million. These related companies are owned by the same person. The Bay property fronts Douglas Street, Blanshard Street, Fisgard Street and Herald Street.
- In 2006, Townline unveiled its plans to preserve the Hudson Bay building and construct multiple tower style buildings on the Bay Parkade.
- In 2007, the restoration and conversion of the Bay building into modern flats, double height lofts, and penthouses commenced. The project known as The Hudson was expected to be ready for occupancy in 2009, with the remaining three towers to be developed afterwards.
- During the economic downturn of 2008/09, progress on the redevelopment of the Bay property slowed.
- In the spring of 2009, BC Housing received an unsolicited proposal from TL Housing Solutions Ltd. (TLHS), formerly Townline Housing Solutions Ltd. TLHS is part of the Townline Group of Companies. These related companies are owned by the same person. In addition, the principal owner of the related company S-8129 Holdings Ltd. (referred to above), is the registered owner of the subject property.

The proposal stated that TLHS would arrange with the landowner to sell a portion of the Bay site (the subject property) to BC Housing to construct a 120 unit mixed affordable rental and home ownership condominium. The building would also include commercial space fronting Fisgard. In return for receiving the property from the landowner at a discounted price, BC Housing would award TLHS with a contract to manage the construction project.

- In September 2009, BC Housing's Executive Committee approved interim construction financing of approximately \$34 million for the construction of the Hudson Mews, a condominium that targets owners/tenants with moderate incomes.

TLHS proposed the units would include high-end finishes consisting of stainless steel appliances, granite counter tops, and hardwood floors. The building would also be equipped with a fitness centre.

The Executive Committee Submission acknowledged that the high-end finishes were "outside the scope of conventional standards for BC Housing" but noted that the increased expenditure would "yield significantly higher rents".

- By early March 2010, BC Housing completed the review of the three submissions in response to the EOI and selected the Greater Victoria Housing Society to own and operate the Hudson Mews. We are advised that BC Housing did not notify the successful proponent following their selection process because they were still in the process of evaluating the financial viability of the project.

Purpose & Scope

We have investigated the concerns raised by both complainants with respect to the Hudson Mews project, in order to assess their legitimacy and report our findings to the Comptroller General.

We examined relevant documentation, including emails, and held interviews with key BC Housing staff and other individuals, as determined necessary.

Executive Summary

We have completed our review of complaints involving the proposed Hudson Mews project.

With respect to the complaint involving the proposed procurement of the former Hudson Bay property we noted that an appraiser retained by TL Housing Solutions overstated the value of the property by approximately \$900,000, based on a subsequent appraisal recommended by the Secretary of Treasury Board.

While the investigation did not find any evidence to support the complainant's allegation that the provincial government was 'bailing out' the owner of the Bay property, we conclude that there was a perceived conflict of interest between the Townline Group of Companies and BC Housing, based on the evidence obtained by the investigation team.

Specifically, IAAS identified several issues which lend support to the perception that BC Housing and TLHS were not operating at arm's length. These issues are described in the body of the report.

We also determined that BC Housing was prepared to go forward with this project despite the fact there were significant unresolved issues with respect to the project's financial viability. Further, BC Housing management knew of these issues, but appeared undeterred in proceeding with the project.

While BC Housing advises us that they had only provided preliminary project approval in September 2009, we noted that the ministry publicly announced BC Housing's commitment to the project in December 2009, despite known concerns with the project's viability.

We do not accept BC Housing's position that the Hudson Mews project would improve the affordable housing situation in Victoria, directly or indirectly. In our opinion, the Hudson Mews project, if carried out as proposed, would expose the province to significant and unnecessary financial risks.

With respect to concerns raised by the ^{15(1)(d)} that TLHS would not follow a public tendering process, we are aware that BC Housing attempted to dispel the Association's concerns but were not successful. We understand the Association's position that there are unresolved questions regarding this project.

We identified additional matters requiring BC Housing management's immediate attention.

- Specifically, we determined that BC Housing's Board of Directors consists of only one member, a Board Chair. Best practices recommend that a governing board should consist of individuals who, collectively, have the required competencies and personal attributes to carry out the Board's responsibilities.
- We also identified ^{s15} ^{s15} which is contrary to BC Housing's Standards of Conduct and can result in conflicts of interest.

Status Update:

On July 21, 2010, BC Housing advised the Ministry of Housing and Social Development that their agency was no longer participating in the Hudson Mews project. The primary reason cited for withdrawing from the project was that the housing development would not deliver the level of affordability for low to moderate-income households as originally intended.

On July 22, 2010, BC Housing updated OCG on its decision to withdraw from the project.

Detailed Support for Conclusion

1.0 Hudson Mews – Procurement of Bay Property/Viability of Project

Background

S-8129 Holdings Ltd., which is a related company to the Townline Group of Companies (as they are owned by the same person) acquired the former Hudson Bay site and announced plans to develop several towers on the site. During an economic downturn that followed this purchase, TL Housing Solutions (a company related to the Townline Group of Companies) submitted a proposal to BC Housing involving the construction of Hudson Mews, a 120 unit residential complex that also included commercial space.

The proposal involved BC Housing providing approximately \$34 million of construction financing, as well as, contracting TLHS, through a direct award, to manage the construction project. In exchange, BC Housing could purchase the undeveloped Hudson Mews site at a significant discount.

In September 2009, BC Housing's Executive Committee approved TL Housing Solutions' proposal, with minor modifications.

BC Housing's executive acknowledged there were some risks associated with the proposal, as it introduced some non-traditional concepts.

We identified issues involving the land purchase, affordability of the units, and compatibility with the crown corporation's corporate goals.

These are discussed below, under sections 1.1 to 1.3.

1.1 Land Appraisal

In the proposal submitted to BC Housing, TLHS reported the land value as \$4,598,000, as the Hudson Mews was considered to be one phase of a multi-phase development.

However, TLHS subsequently increased the assessed value of the subject property to \$4,827,442, citing they had incorrectly understated the land's value.

BC Housing considered the revised value in the Executive Committee submission noted above.

On December 9, 2009, based on a statement made by the President of the Townline Group of Companies to the media, it was reported that the subject property would be purchased for \$4 million, or at 80% of its actual market value.

We noted the following issues:

- TLHS proposed that BC Housing could acquire the land from Townline Victoria. However, S-8129 Holdings Ltd., not Townline Victoria, owns the property.

Regardless, these are related companies, which are both owned by the same person.

- IAAS determined that the land value is more appropriately valued at a price point between the BC Assessment Authority's value of approximately \$2.5 million and TLHS's original appraisal of \$4.6 million.
- On February 18, 2010, the Secretary to Treasury Board advised BC Housing to commission an independent appraisal of the land based on the Hudson Mews being a stand-alone development. The assessed value, following the Secretary to Treasury Board's recommendation, was \$4,088,599.

Conclusion

TLHS overstated the market value of the Hudson Mews property in its proposal to BC Housing by approximately \$900,000.

This overstated value led to a public perception that the province was receiving a one million dollar discount on the land purchase, whereas it was actually receiving a discount of less than \$100,000 in exchange for direct awarding a contract to manage the Hudson Mews project to the landowner's related company (TLHS).

In our opinion, BC Housing did not exercise the appropriate level of diligence in assessing the land value, prior to approving the Executive Committee Submission.

In view of the issues surrounding the land's appraised value, we did not believe it was in the province's best interest for BC Housing to be involved directly or indirectly in the purchase of the land at the value stated in the Executive Committee Submission approved by BC Housing's Executive Committee.

1.2 Affordability

The proposal submitted by TLHS recommending BC Housing finance the construction of the 120 unit rental and home ownership condominium complex included one bedroom, one bedroom plus den, and two bedroom units ranging from 550 to 840 square feet.

The Executive Committee Submission proposed the discounted rents would range from \$1,135 to \$1,598.

The discounted sale prices for the homeownership units (i.e. 90% of market value) would fall between \$247,104 and \$358,560.

Hudson Mews would be marketed as an affordable housing complex for low to moderate household income earners (i.e. up to \$57,977 in 2009 and up to \$61,223 in 2010).

The Executive Committee Submission proposed a mix of 80 rental units and 40 home ownership units.

We noted the following issues:

- An internal analysis performed by BC Housing staff concluded that an 80 rental unit and 40 home ownership unit mix was not financially viable.

BC Housing staff determined that the appropriate mix was 40 rental units and 80 home ownership units.

Evidence indicates that this information was available to BC Housing Executive before the Executive Submission was completed and submitted, but was not acted upon.

- An internal analysis performed by BC Housing staff concluded that the maximum sales price for a unit should be \$243,691, based on permissible household incomes (\$57,977 in 2009), required down payment (\$25,000), 35 year amortization period, 5% interest rate and other applicable costs (condo fees, property taxes, heating costs etc.).

The sales price determined by the BC Housing staff was lower than the proposed range included in the Executive Submission noted above (\$247,104 to \$358,560).

Evidence indicates that this information was available to BC Housing Executive before the Executive Submission was completed and submitted, but was not acted upon.

- An internal analysis performed by BC Housing staff identified additional issues with the proposed rents, as follows:
 - Some proposed rents exceeded the maximum allowable rent (30% of the second quintile or \$57,977).
 - Proposed rents were significantly higher than the average market rent in Victoria, and more specifically in downtown Victoria (the best comparable).
 - The predicted demand for high-end rental units, as proposed by the Hudson Mews project, would be low, as there would be a large supply of newly completed projects coming onto the market when the Hudson Mews was scheduled for completion.

Evidence indicates that this information was available to BC Housing Executive before the Executive Submission was completed and submitted, but was not acted upon.

Conclusion

BC Housing approved the Executive Committee Submission for the Hudson Mews proposal despite the fact there were known affordability concerns that significantly affected the financial viability of the project.

Such concerns involved the proposed sales prices, rental rates, and the appropriate mix of rental versus sales units.

In our opinion, approval of this project as proposed and approved exposed the province to significant and unnecessary financial risks.

1.3 Corporate Goals

The BC Housing's Business 2009/10 Corporate Business Plan identifies four Corporate Goals and Objectives.

Two of these goals indicate a strategy to identify British Columbians who are considered most in need.

While the Executive Committee Submission acknowledges that the Hudson Mews project does not address Victoria's core-housing needs, it indicated that the project would generate positive cash flows that could be applied to homelessness projects.

BC Housing Executive also advised IAAS that approval of the Hudson Mews project would improve the affordable housing situation in Victoria by creating vacancies in the lower rental market as people moved into the Hudson Mews complex.

Conclusion

BC Housing acknowledged that the Hudson Mews project would not directly improve the affordable housing situation in Victoria, and as such did not align to its primary target of assisting British Columbians most in need.

We believe entering into this type of arrangement not only conflicts with the crown corporation's mandate but gives the appearance of a speculative real estate investment involving an unnecessary transfer of risk from the private sector to the public sector.

2.0

s15(1)(d)

Concerns

Background

As noted earlier in the report, OCG was contacted by the s15(1)(d) who expressed their concerns about the tendering of contracts related to the Hudson Mews project. We reviewed relevant documentation, including emails, and noted the following:

- BC Housing informed us that s15(1)(d) concerns were premature and that they had meaningful discussions with TLHS regarding the competitive bid process.

We confirmed that BC Housing did provide an information session for s15(1)(d)

However, as s15(1)(d) representative informed us that their concerns have not been satisfactorily resolved. Specifically s15(1)(d) expressed concerns with BC Housing's lack of transparency and fairness in their procurement practices.

We obtained evidence, which states that BC Housing does not subscribe to full government procurement practice for their financing. Further, BC Housing advised us that the province's Capital Asset Management Framework (CAMF) clearly supports innovative strategies with respect to financing procurement projects.

- There is email evidence from TLHS to BC Housing, which suggests that the Townline Group of Companies are not required to use a bid depository, nor are they required to go to public or invitational tendered. The email further states that 90% of the construction of the Hudson Mews would be tendered, but not publicly.

We noted that TLHS informed BC Housing that an RFP process would be utilized to solicit bids, whenever possible.

BC Housing, as the financier for the Hudson Mews project, advised IAAS that it would have the right to oversee the construction project, including the tendering process.

Conclusion

Based on our review of relevant documentation, including emails, we believe s15(1)(d) concerns with respect to TLHS's intention to secure contracts for the Hudson Mews project through a public tendering process have merit.

Although s15(1)(d) acknowledges that TLHS provided an information session for this specific project, s15(1)(d) advised us that their key concerns remain unresolved. We believe their concerns have merit.

3.0 Additional Matters Requiring Attention

During our fieldwork, we identified the following issues that require BC Housing management's attention.

3.1 Board Governance

In February 2005, the Board Resourcing and Development Office (BRDO) of the Premier introduced the *BC Governance and Disclosure Guidelines for Governing Boards of Public Sector Organizations* (the "*Best Practices Guidelines*") which establishes broad provincial standards for board governance practices.

At this time, BC Housing's Board of Directors consists of only one member, the Board Chair.

The BRDO suggests that an appropriate Board size is 9 to 11 members, unless otherwise required by legislation or directed by Cabinet. The Board should consist of a group of individuals who have the appropriate combination of competencies and personal attributes to support the organization's mission and contribute together as a highly motivated team.

Board members that are appropriately selected and appointed provide a valuable oversight role for any organization, particularly one as critical and politically sensitive as BC Housing. Further, an effective board enhances accountability and provides stakeholders with greater assurance that sound business decisions are made that not only meet the organization's objectives, but also consider unnecessary exposures to significant risks.

We do not believe that a single board member, regardless of his/her experience and expertise, can effectively provide the required oversight for an organization such as BC Housing.

Recommendation

BC Housing should adopt best practices as recommended by the *BC Governance and Disclosure Guidelines for Governing Boards of Public Sector Organizations*. Specifically, BC Housing should operate with a Board of Directors that is made up of qualified individuals who collectively enhance the agency's accountability, as well as provide valuable oversight.

3.2

s15

We determined that BC Housing staff are not complying with its Standards of Conduct Policy

s15

We obtained a copy of BC Housing's 2007 Standards of Conduct Policy that clearly articulates the behaviours expected of employees and directors of the board.

The policy states that compliance with the standards is mandatory in order to maintain and enhance the public's trust and confidence in BC Housing. For example the policy states:

- all those who do business with BC Housing, as contractors or customers, must have access to BC Housing on equal terms; and

s15

We discussed these practices with certain staff, including BC Housing's Executive Director of Human Resources and advised these individuals ^{s15} was contrary to BC Housing's Standards of Conduct. Nonetheless, staff interviewed acknowledged suppliers do offer gifts to BC Housing staff as a normal course of business.

Some staff admitted they would appreciate more direction in this area.

s15

Recommendations

We recommend BC Housing revisit its Standards of Conduct Policy. Specifically, BC Housing Management should take immediate action to clarify and communicate their policy to all staff, as well as enforce compliance with the policy. The practice of

s15

should be discontinued immediately.

If you require additional information or clarification on any areas in this report, please contact me at (250) 387-8198 or Dan Peck at (250) 387-8542.



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