CALGARY
ASSESSMENT REVIEW BOARD
DECISION WITH REASONS

In the matter of the complaint against the property assessment as provided by the *Municipal Government Act*, Chapter M-26, Section 460, Revised Statutes of Alberta 2000 (the *Act*).

between:

OPTRUST OFFICE INC., COMPLAINANT,
as represented by ALTUS GROUP LIMITED

and

The City Of Calgary, RESPONDENT

before:

T. Helgeson, PRESIDING OFFICER
J. Kerrison, MEMBER
B. Jerchel, MEMBER

This is a complaint to the Calgary Assessment Review Board in respect of a property assessment prepared by the Assessor of The City of Calgary and entered in the 2012 Assessment Roll as follows:

ROLL NUMBER: 200737708

LOCATION ADDRESS: 607 8th Avenue SW

HEARING NUMBER: 67085

ASSESSMENT: $78,960,000

This complaint was heard on August 23, 2012 at the office of the Assessment Review Board located at Floor Number 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 2.

Appeared on behalf of the Complainant:

- *S. Meiklejohn*

Appeared on behalf of the Respondent:

- *A. Czechowskyi*

Board's Decision in Respect of Procedural or Jurisdictional Matters:

[1] At the commencement of the hearing, both parties agreed that all questions and answers from previous hearings should apply to the present complaint. The Respondent further requested that all decisions submitted in previous hearings also apply. The Board consented to the joint request, and there being no objection from the Complainant, the Board also consented to the Respondent's request with respect to decisions submitted in previous hearings.

[2] As in the three complaint hearings that preceded the present hearing, it was understood by the parties and the Board that relevant argument and evidence from the previous hearings would be brought forward and considered in the present case.

Property Description:

[3] Assessed at $78,960,000, the subject property, known as "Plains Midstream Plaza" is a 10 storey downtown office building located at 607 8th Avenue SW in the DT2 economic zone of downtown Calgary. Constructed in 2007, the subject property has been assessed as a Class "A-Old" building. The assessment is based on the income approach, with a capitalization rate ("cap rate") of 6.75%. The assessment is $325.79 per sq. ft.

Issues:

[4] The Board found the determinant issues in this complaint to be as follows:

1. Is the subject property sufficiently similar to A- buildings to warrant its reclassification from "A-Old" to A-.

2. Should the assessed value of the office space be reduced from $22 per sq. ft. to $16 per sq. ft.?

3. Should the assessed value of the retail space be reduced from $25 per sq. ft. to $20 per sq. ft.?

4. Should the vacancy allowance, 4.0% as assessed, be increased to 10.0% for all types of space other than low profile space?

5. Should the assessed parking rate be reduced to $425 from $475?

6. Should the capitalization rate of 6.75% be increased to 7.50%?

Complainant's Requested Value: $45,600,000

Summary of the Complainant's Submission

Building Quality Class, and Requested Assessment

[5] The assessment amount is incorrect. The primary issue is the quality classification of the subject property, i.e., A-Old. The "A-2" class is equivalent to A-Old. The subject property was classified as A-Old based on income. The Respondent has not relied on typical market conditions. The subject property should be reclassified as an A- building. The difference is this: A-Old buildings are assessed at $22 per sq. ft., and A- buildings are assessed at $20 per sq. ft. Because we are requesting a reclassification to A- for the subject property, the same arguments and evidence apply as in the hearings for file numbers 67824 and 67825.

[6] Basic to our requested assessment at p. 59 of Exhibit C-1, are market value, and fairness and equity. There are concerns with valuation, and the characteristics and physical condition of the building. The requested assessment was originally $55,470,000. This has been revised to $45,600,000, or $189.15 per sq. ft., based on office space at $16 per sq. ft., retail space at $20 per sq. ft., vacancy at 10.0%, parking at $425 per stall, and a cap rate of 7.50%.

Property Characteristics

[7] The subject property has 10 storeys, and 241,059 sq. ft. of floor space. It is a small building, comparatively. A typical class A building has 350,000 to 600,000 sq. ft. of floor space. The subject is a glass curtain wall building, with no marble, or significant design features. With only 76 parking stalls, the subject has a parking ratio of 1/3200. The typical downtown ratio is 1/2000.

[8] Only 12,316 sq. ft. of the subject property, i.e., 5.0%, is devoted to retail. Vacant space in the subject property is currently at 8,000 sq. ft, the result of failure of a restaurant named "7". The subject has no amenities, i.e., no gym, or open area, etc. The subject property is a "plain Jane" building. Space in the subject property competes with other, similar buildings in the area. It is not presently connected to +15, and won't be until "Eighth Avenue Place" is completed.

Comparison with Other Buildings in the Vicinity

[9] As an A-Old building, the subject property is in good company. For example, Western Canadian Place at 701 8th Avenue SW, and Encor Place at 645 7th Avenue SW. Western Canadian Place, constructed in 1981, is, like the subject, located in DT2 and classified A-Old. It has a floor plate of 18,400 sq. ft., is connected to +15, and has two office towers with up to 41 storeys. Floor space totals 1,099,056 sq. ft., 8,227 sq. ft. of which is retail space. There is substantial parking in the Centennial Parkade and the Yale parking lot.

[10] Constructed in 1987, Encor Place is also located in DT2. Encor Place has 29 storeys (the subject has only 10), a floor plate of 13,800 sq. ft., and a total area of 358,846 sq. ft., 1,604 sq. ft. of which is retail space. Encore Place is connected by +15 to the J. J. Bowlen building, and

its parking ratio is 1/3300.

[11] The subject property is dramatically smaller than either Encore Place or Western Canadian Place, but size of floor plate and the amount of parking are not major determinants of A class buildings, nor is age. The primary determinants are floor area, and massiveness of the building. The subject property is more similar to A- buildings than A-Old.

Differentials between Building Classes and Economic Zones

[12] As mentioned above, much of the same argument and evidence submitted in the hearings in file numbers 67824 and 67825 apply here. In its assessments of A- buildings, the Respondent does not differentiate between rental rates in A- buildings in DT1, and A- buildings in DT2, but the Respondent does recognize a differential in rental rates between B class buildings in DT1 and B class buildings in DT2. It is submitted that a similar differential must necessarily exist with respect to A- buildings in DT1 and DT2.

Rental Rates

[13] Pages 15 and 16 of Exhibit Part I, C3A show that the weighted averages of A- office rents in DT1 and DT2 are $21.48 and $18.61, respectively. Nevertheless, Local Assessment Review Board decisions found there was no significant difference between DT1 and DT2. It is respectfully submitted that 15.0% is a significant difference. With renewals removed, the office rate in DT2 drops to $15.96, very close to what we are asking for the subject property as an A- building: $16 per sq. ft.

Property Classification and Capitalization Rates

[14] If the benchmark capitalization rate ("cap rate") for "AA" buildings is 6.8%, the cap rate should be higher for a A- buildings to reflect greater risk. Clearly, the subject property is not comparable to Bankers Hall.

Valuation Parameters, Parking, and Requested Assessment

[15] In summary, valuation should be based on the characteristics and physical condition of the building. Based on reclassification from A-Old to A-, the assessed rate for office space in the subject property should be reduced from $20 to $16 per sq. ft. Retail space should be no more than $20 per sq. ft. The office vacancy rate should be increased from 4.0% to 10.0%, and the parking rate reduced from $475 to $425, to reflect the difference between DT1 and DT2. Finally, the cap rate should be 7.5%, not 6.75%.

Economic Zones, Vacancy, and Rents

[16] The Respondent's A- rent survey should have reflected the Respondent's vacancy survey, i.e., the rent survey should have been divided between economic zones DT1 and DT2. When vacancies go up, rents go down, and vacancies are higher for A- buildings in DT2 than in DT1. That implies rents will be lower in DT2.

Sales and Capitalization Rates

[17] To be relied upon for assessment purposes, sales should be at arm's length. With respect

to the two Scotia Centre sales that occurred in April, 2011, i.e., within the valuation period, the only valid sale is the one for the first 50% interest. It was purchased by Scotiabank from Aspen, and it was a straight cash sale. The resulting cap rate is 7.50%. The other Scotia sale is unreliable; Scotiabank lent Homburg (a REIT) the money to make the purchase, and Scotiabank induced the sale. Homburg also got the lucrative management contract.

[18] The sale of Gulf Canada Square occurred on September 2nd, 2011, two months *post facto*. As mentioned above, the general rule is that you do not use *post facto* sales other than for testing an assessment, and only when the sales are time-adjusted. Included in the Gulf Canada sale was the right to use 240 parking stalls in the adjacent City of Calgary parkade. The Respondent did not use the income from the parking stalls in the assessment of Gulf Canada Square, but had they done so, the cap rate would have been greater than 6.39%. That said, the only valid sale of a Class A building is the one between Scotiabank and Aspen.

Assessment-to-Sales Ratios and Vertical Inequity

[19] There is something inconsistent with respect to how downtown A and AA class buildings, and downtown B and C class buildings are assessed. An analysis of assessment-to-sales ratios ("ASRs") for 37 AA, A, B and C class buildings produced a mean ASR of 0.654, and a median ASR of 0.586. For Class AA and A buildings, the mean ASR is 0.979, and the median is also 0.979. This indicates vertical inequity in assessment. This puts A buildings at a disadvantage with respect to all the B and C buildings in downtown Calgary. The request is to place A- buildings like the subject property in line with B buildings

Summary

[20] In sum, when you separate A- class properties by their economic zones, DT1 and DT2, the typical office rental rate for the subject property turns out to be $16 per sq. ft., not $20. Although the Respondent recognizes that there is a difference in vacancy rates between DT1 and DT2, it fails to recognize a difference in rents. During the assessment year, the vacancy in the subject property was 0.5%. There should also be a difference in the parking rates between DT1 and DT2. Finally, the cap rate should be 7.5%, not 6.75%. These adjustments will solve the inequity, and result in the requested assessment.

Summary of the Respondent's Submission

Net Operating Income, and Cap Rate

[21] The assessment is at $325 per sq. ft. The Respondent is asking for $189.00 per sq. ft., with no supporting sales. If net operating income goes up, the cap rate goes up. The Complainant is asking the Board to take a cap rate developed from rental rates of $24 to $25 per sq. ft., and apply it to a rate of $16 per sq. ft. If the Board is convinced that the rental rate should be $16 per sq. ft., the cap rate will require adjustment.

Rent and Building Quality

[22] At pp. 61 of Exhibit C-1 you will find a summary of the rent roll of the subject property. It shows rent of $25 per sq. ft. from a lease that commenced July 1st, 2011. The subject property is connected to Eighth Avenue Place, an AA class property. Retail space in the subject is at $25 to $28 per sq. ft., but the primary driver of value is office space. The assessed rate of $22 per

sq. ft. is well founded. The assessed retail rate has not been disputed by the Complainant. As for parking, there is plenty available at Centennial Parkade and Eight Avenue Place.

[23] At pp. 208 and 209 of Exhibit C-1 there is a table showing assessments of 16 A-Old buildings. The mean assessed value is $331.69 per sq. ft., very close to the assessment of the subject property at $325 per sq. ft. The subject is located in a desirable area; Eighth Avenue Place is right next door. At p. 18 of Exhibit R-1 there are 42 Office Class A rent equity comparables. The average of rental rates for all leases of space over 10,000 sq. ft. is $21.83 per sq. ft.

The Scotia Centre Sales, and Gulf Canada Square

[24] In the "straight cash" deal, i.e., the sale from Aspen to Scotiabank, Aspen had the right of first refusal. The first sale was not put on the market, but the second sale was. There is no evidence of the second sale being subject to undue elements.

[25] Gulf Canada Square does use part of the City of Calgary's parkade, but the income stream from those stalls goes to the City, not Gulf Canada Square

Assessment to Sales Ratios

[26] The sales of Banker's Hall and Suncor Energy Centre indicate a mean and median cap rate of 6.80%. The ASRs are very close to 1. This supports the 2011 cap rate for A- properties, for there have been no other sales to support a change.

Summary of the Complainant's Rebuttal

Basic Questions

[27] An AA class building has a cap rate of 6.25%, as assessed. Both A and A- buildings have an assessed cap rate of 6.75%, as does an A-Old. A class buildings are given a cap rate of 6.75% regardless of "old" or "new".

[28] There are only three Class A buildings in DT2. There isn't sufficient data except for the Encor building and Western Canadian Place. The only true sale is the first sale of Scotia Centre. The average of five Scotia Centre leases at p. 18 of Exhibit R-1 show a range of $17 to $21 per sq. ft., an average of $19.90 per sq. ft. and a median of $21 per sq. ft.

[29] The basis of the Scotia Centre cap rate of 7.36% is a $22 per sq. ft. rental rate. If the cap rate is 6.75, a $20 per sq. ft. rental rate could apply. The average of seven Scotia Centre leases (at p. 18 of Exhibit R-1) show a median of $18 per sq. ft. If income from the two smaller buildings in Scotia Centre are included, the cap rate becomes 6.86%.

[30] For all the A class buildings in Calgary, either the rent is too high, or the cap rate is too low by .05. Encor Place is the building most similar to the subject property. Is the subject property equal or better than Encor Place? Page 18 of Exhibit R-1 shows a weighted mean of $20.94 per sq. ft. for downtown A class buildings.

[31] The assessment fails to reflect a difference in rents between DT1 and DT2. The only difference with the two previous complaints is the A-Old classification of the subject property.

The Respondent's own evidence indicates all Class A buildings are over-assessed at $22 per sq. ft. Either increase the cap rate, or reduce the rent. The Respondent's rent is too high, and their cap rate is too low.

[32] The subject property has a floor plate of 20,372 sq. ft., and the floor area is only 241,059 sq. ft. Compare the subject to Shaw Court. Shaw Court is a sandstone building, with a glass atrium. Encor is a marble building, with +15 connection. The subject's classification should be A-.

Inconsistency

[33] There is inconsistency in how downtown A and AA buildings are assessed in comparison to downtown B and C class buildings. An analysis of ASRs for 37 AA, A, B, and C class buildings produced a mean ASR of 0.654, and a median ASR of 0.586, but for AA and A class buildings, the mean, as well as the median, ASR is 0.979. This indicates an inequity in assessment that puts the subject property and other A class buildings at a disadvantage with respect to the B and C class buildings in downtown Calgary. The request is to place A- buildings in line with B buildings.

Simple Facts

[34] The simple fact is this: when you stratify the A- properties by their economic zones, DT1 and DT2, the typical office rental rate for the subject property becomes $16 per sq. ft., not $20. The Respondent recognizes that there is a difference in vacancy rates between DT1 and DT2, but somehow or another, fails to recognize a difference in rents.

[35] A difference in parking rates between DT1 and DT2 also needs to be recognized. And finally, the cap rate, presently 6.75%. should be 7.50%. These adjustments will solve the inequity, and produce the requested assessment.

Board's Findings in Respect of Each Matter or Issue:

Building Classification

[36] A great deal hinges on the Board's decision regarding the classification of the subject property. According to the Complainant, the primary determinants of building quality are floor area, and massiveness. Other factors mentioned are floor area, gyms, open areas, and +15. What is lacking in the Complainant's evidence is a crisp delineation of the various building quality classes, i.e. A, A-Old, A-, and B. This seems to be a chronic problem whenever the issue of building classification arises. Comparison to buildings with other classifications might substitute for delineation, but providing adequate details of the building features of the comparables would be *sine qua non*. The Board finds there is insufficient evidence to support changing the classification of the subject property from A-Old to A-.

Sales and Cap Rates

[37] The Complainant submits that the cap rate of 6.75% for the assessment of the subject property does not adequately reflect its risk as a lesser property when the benchmark for AA buildings is 6.8%. The answer is that the cap rate should be derived from arm's-length sales and net operating income, not by comparison with cap rates used in assessing other building

classes. The evidence shows that there were only two sales of an A class office building in DT1 during the agreed-upon valuation period, i.e., the period from July 1st, 2010 to July 30th, 2011. Both sales were of Scotia Centre at 225 7th Avenue SW, and both occurred on the same date, April 21st, 2011.

[38] Each sale was for a 50% interest. In one transaction, the vendor was Aspen Properties, the purchaser Scotiabank, and the sale price was $95,000,000. At the same time, Scotiabank sold a 50% interest in Scotia Centre to Homburg Canada REIT GP for $116,000,000.

[39] The Complainant submits that the sale from Scotiabank to Homburg Canada was "bad" because Scotiabank lent Homburg the money for the purchase and brokered the sale, but insists that the sale from Aspen to Scotiabank for $95,000,000 was a straight cash deal, hence a valid sale that supports a non-typical cap rate of 7.40%, and a cap rate (as assessed) of 6.50%. The Respondent submits that the Aspen to Scotiabank sale was not brokered, therefore unreliable as an indicator of fair market value.

[40] Another sale that was considered was one that occurred in September, 2011. This was the sale of Gulf Canada Square, an A class building, which has an assessed cap rate of 6.75%. In addition to the sale being *post facto*, the Respondent's evidence was that there was a right of first refusal. The Complainant submits that had the parking stalls been included in the assessed value, the cap rate would be more than it is as assessed, thus supporting the Complainant's argument for a higher cap rate for the subject property. This ignores the fact that the parking stalls are leased from the City of Calgary, and the Board can but wonder how much more the lessee could charge for parking over and above what it is paying the lessor.

[41] The Board finds that the above sales are hardly characteristic of what might be called a universe of sales, and concludes that none of the sales are sufficiently trustworthy to ground a valid cap rate. In the absence of substantive, probative evidence, the cap rate used in the assessment of the subject property is confirmed at 6.75%.

Vertical Inequity

[42] With respect to the Complainant's argument that there is "vertical inequity" between A class buildings with ASRs approaching 1.00, and B class buildings whose ASRs are in the 0.5 range, the Board agrees that the inequity should be remedied, but not in the manner contemplated by the Complainant, i.e., to reduce the assessments of A buildings so their ASRs would approximate those of B buildings. That would only worsen the problem, and result in further breaches of s. 10(3) of the *Matters Relating to Assessment and Taxation Regulation* ("MRAT").

Vacancy

[43] The assessed vacancy rates for A-Old buildings in DT2 are 4.0% for office space, and 6.0% for retail space. The assessed vacancy rate for the classification of A- in DT2 is 9.0%. The Complainant requests 10.0% for all classes of space in the subject property. The Board finds that the Complainant's request is based largely on reclassification to A-. The vacancy rates for space in the subject property will remain as assessed.

[44] As assessed, the parking rate for the subject is $475 per stall, the same rate that applies to A- buildings. Information from a third party, Cresa Partners, at pp. 120 and 121 of Exhibit C-1 indicates that the actual parking rates for A-Old buildings, both reserved and unreserved, are somewhat higher that the assessed rate of $475 per stall. In the result, the Board found insufficient evidence to support an adjustment in the assessed parking rate, and the assessed parking rate is confirmed at $475 per stall.

Rental Rates

[45] The Complainant submits that rents in the subject property, i.e., as an A- building in DT2, should be less than rents in A- class buildings in DT1. In support of this argument, the Complainant refers to a table at pp 15 and 16 of Exhibit Part I, C3(a), which shows all office leases that commenced during the valuation year in A- buildings in DT1 and DT2. The A- leases in DT1 reveal a mean of $20.66 per sq. ft., and a weighted average of $21.48 per sq. ft. The mean for the leases in DT2 is $16.97 per sq. ft., and the weighted average is $18.61 per sq. ft. The Board agrees that this evidence appears to indicate a significant difference in A- rental rates between DT1 and DT2.

[46] Nevertheless, the subject property remains an A-Old building, and there is no evidence to show a similar difference between A-Old buildings in DT1 and in DT2. The Board found insufficient evidence to support an adjustment to the rate as assessed. The Board also found there was no evidence whatsoever with respect to retail rents.

<u>Board's Decision:</u>

[47] The assessment is confirmed at $78,960,000.

DATED AT THE CITY OF CALGARY THIS 7th **DAY OF** November **2012.**

[redacted]

Presiding Officer

<u>Exhibits</u>

C-1, Complainant's Evidence Submission

R-1, Respondent's Assessment Brief

C-2, Complainant's Realnet Reports

Part I, C-3(a), Complainant's Rebuttal Submission

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Appeal type	Property type	Property sub-type	Issue	Sub-issue
CARB	Office	High Rise	Income Approach	Land & Improvement

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An appeal may be made to the Court of Queen's Bench on a question of law or jurisdiction with respect to a decision of an assessment review board.

Any of the following may appeal the decision of an assessment review board:

(a) the complainant;

(b) an assessed person, other than the complainant, who is affected by the decision;

(c) the municipality, if the decision being appealed relates to property that is within the boundaries of that municipality;

(d) the assessor for a municipality referred to in clause (c).

An application for leave to appeal must be filed with the Court of Queen's Bench within 30 days after the persons notified of the hearing receive the decision, and notice of the application for leave to appeal must be given to

(a) the assessment review board, and

(b) any other persons as the judge directs.