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:

1183044 Alberta Ltd. And 1023820 Alberta Ltd. (as represented by Altus Group), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

W. Kipp, PRESIDING OFFICER
R. Cochrane, MEMBER
J. Rankin, 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 2011 Assessment Roll as follows:

ROLL NUMBER:	**068 241 793**
LOCATION ADDRESS:	**751 – 3 Street SW, Calgary AB**
HEARING NUMBER:	**64013**
ASSESSMENT:	**$363,130,000**

This complaint was heard on the 27th day of July, 2011 at the office of the Assessment Review Board located at Floor Number 3, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 10.

Appeared on behalf of the Complainant:

- *D. Genereux*

Appeared on behalf of the Respondent:

- *W. Krysinski and H. Neumann*

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

There were no preliminary or jurisdictional matters to be decided.

Property Description:

Calgary Eaton Centre (The Core)/Canada Trust Tower – a retail and office complex that occupies all of a small downtown block bounded by 7th and 8th Avenues and 3rd and 4th Streets SW. A 40 storey office building rises above a four level retail podium, all completed in 1989. In 2010/2011, a major renovation/upgrading of the retail component was completed. The retail floors, originally known as Calgary Eaton Centre are directly linked to the Holt Renfrew building (west side of 4 Street SW) and to the Toronto Dominion (TD) Square retail (east side of 3 Street SW). The TD Square retail was also completely renovated/upgraded at the same time as that in the subject and the combined three and four levels of retail space have been named "The Core." Bridges over 3 Street and 4 Street that link the three properties at the +15 and +30 levels are wide and they are developed with retail stores as well.

The Canada Trust office tower contains 617,248 square feet of office space. The average floorplate size is 15,431 square feet. In the retail podium, floor areas are:

Food Court:	5,019 square feet
1st Floor Retail:	30,165 square feet
2nd Floor Retail:	34,653 square feet
3rd Floor Retail:	37,525 square feet
4th Floor Retail:	12,388 square feet

There are 34,712 square feet of storage space in the complex and there is an underground parkade with 293 parking stalls.

For 2011, the property is assessed using an income approach. In the assessment calculations, rents for offices (Class AA) are $30.00 per square foot. Retail spaces are attributed rental rates ranging from $25.00 to $90.00 per square foot while food court spaces are at $150.00 per square foot. Storage space is assigned a rent of $12.00 per square foot. Parking stall rent is set at $525 per stall per month.

The total assessment of $363,130,000 represents a unit rate of $470.37 per square foot of gross building area (excluding the parkade).

Issues:

There were numerous grounds for appeal set out in the Assessment Review Board Complaint form that was filed on March 4, 2011. At the hearing, however, the Complainant pursued just three issues:

1. Office rent rate should be $27.00 per square foot rather than $30.00;
2. The areas of retail space are incorrect and should be corrected to match areas shown on the rent roll;
3. The capitalization rate used in the income approach is too low and should be increased from 6.75% to 7.0%

Complainant's Requested Value: $323,946,000

Party Positions on the Issues:

Complainant's Position:

1. Office rent rate

The issue of the office space rental rate in Class AA buildings had been raised at prior 2011 CARB hearings. CARB decisions were rendered wherein the $30.00 per square foot rate was confirmed. For this hearing, the Complainant still maintained that the rate should be reduced to $27.00 per square foot but stated that there is no need to present the full argument and evidence that had been heard at prior hearings. All of the evidence and argument is included in Complainant's brief marked Exhibit C1. The Board is requested to read and consider this material.

2. Retail space allocation

A table in Exhibit C1 compared floor areas pursuant to information in a rent roll to the areas upon which the assessment is based. There are variances in all but three areas. A copy of a part of the rent roll was included to support the "correct" areas in the table. The Complainant recalculated the 2011 assessment on the basis of only the space allocation argument, arriving at a reduced assessment of $361,753,373.

3. Capitalization rate

Most Class AA office properties in downtown are assessed by the income approach utilizing a capitalization rate of 7.0%. All income approach input factors are the same for the subject except for some retail rent rates and the capitalization rate which is 6.75%.

The Complainant argued that the assessor's reduced capitalization rate was influenced, in part at least, by the capitalization rate for regional shopping centres which is 6.5%. Yet, the subject with just 155,000 square feet of retail space is significantly smaller than a regional shopping centre which can contain 1,000,000 or more square feet. The amount of space in the subject is more closely aligned with Power Centres or Community Centres which are assessed by use of a 7.25% capitalization rate. The 6.75% capitalization rate is applied to all income from the subject property, including office, parking, storage and retail space income. The resulting tax on the entire property is higher than all of the competitor AA buildings in downtown.

There is no basis for the lower capitalization rate because there have been no sales of similar properties from which the capitalization rate might have been extracted. In fact, there have been no downtown office property sales since 2006. With no market support, there is no basis for the arbitrary 0.25% capitalization rate reduction from that used for other AA properties.

The 2010 assessment year was the first year that the capitalization rate adjustment was made for the subject and a few similarly located properties on the Stephen Avenue (8^{th} Avenue) Mall with a higher than normal ratio of retail space. The amount of income generated by the subject retail space is still only a small portion of the total income including that from office, storage and parking components. In 2010, the assessor had rationalized the capitalization rate adjustment by a comparison to regional shopping centres, however, there are significant differences in the amounts of retail area.

A number of real estate brokers and analysts prepare periodic reports that include information on capitalization rates. None of these industry reports state that properties such as the subject have a different capitalization rate than other properties in the same class. Both Altus Insite and CB Richard Ellis reported average capitalization rates for AA offices at 7.0% for the second quarter of 2010.

Respondent's Position:

1. Office rent rate

Exhibit R1 entered into evidence by the Respondent also provided substantial argument and evidence regarding office rent rates for AA space in downtown. The Respondent took a similar position to that of the Complainant regarding this issue. The evidence is there for the benefit of the Board and there would be nothing to be gained by having oral presentations on an issue that has been heard previously and decided upon by the Calgary CARB.

2. Retail space allocation

The assessor assesses property such as the subject based on information provided by the owner through the ARFI (Assessment Request For Information) process. Included in owner provided information is data on floor areas, tenant leases and so on. If there are changes in things such as floor area allocations from time to time, the onus is on the owner to update the assessor's information.

In the subject instance, the assessment was based on the floor area information that the assessor had at the time of preparing the assessment. If there were changes to be made, the owner has opportunities to have them made during the complaint period (typically January to March) or during consultation periods (typically October). There does not have to be a complaint made against the assessment to get floor areas corrected. The Respondent undertook to make necessary changes for next year's assessment.

3. Capitalization rate

There is a group of Class AA, A and B properties that front onto the Stephen Avenue (8th Avenue) Mall that have higher than typical ratios of retail space (as much as 20% in some buildings compared to a typical 2% to 4%). For these properties, assessments are made using the income approach wherein the capitalization rate is reduced by 0.25%. This practice started in 2010 after a number of complaints had been filed wherein the issue was that typical office buildings were being treated unfairly because they were less valuable than those with high ratios of retail space but were valued with the same capitalization rates. Although there had been no sales of major downtown properties for several years, the Respondent opined that when there were sales, the market did differentiate between those containing significant retail space and those with a typical ratio. In the opinion of the Respondent, properties such as the subject are superior investments due to greater security of income and thus, lower ownership risk due to the significant retail component. The 0.25% capitalization rate reduction takes this lower risk into account.

A chart in Exhibit R1 showed a number of properties that were assessed in the manner described above, including Bankers' Hall (AA), Scotia Centre (A), TD Square (A) and the subject (AA). For comparison, three regional shopping centre assessments were summarized wherein the capitalization rate was 6.5%.

The Respondent provided data on three historical (2006) sales. Scotia Centre (Class A) sold exhibiting a 5.15% capitalization rate. A Class B building at 940 – 6 Avenue SW sold at a capitalization rate of 6.8% and a suburban office property sale at 8500 Macleod Trail SW showed a 7.5% capitalization rate. These sales showed that the market attributed a lower capitalization rate for properties on the Stephen Avenue Mall with high retail space components. An April 2011 sale of a 50% interest in Scotia Centre indicated a capitalization rate of 7.4%. If the sale was analyzed using 2010 rental rates, the Respondent stated that the capitalization rate would have been 6.5%.

CARB decision 0585/2010-P was copied in Exhibit R1 and the Respondent drew the attention of the Board to this and other decisions.

Part of the Respondent's argument was that, "at some point, you need to compare the assessment to the market." This statement pertained to support for the 2011 assessment as well as to the assessment being requested by the Complainant.

The subject assessment reflects a rate of $470 per square foot of building area and the Complainant's request is to have the rate reduced to $420 per square foot. Respondent support for the assessment of $470 per square foot came from an analysis of recent events involving office properties. Three events involved transfers of partial interests in Class AA and A buildings (Bankers' Hall, Suncor Energy Centre and Fifth Avenue Place) from owners to REITs (Real Estate Investment Trusts) that were controlled by the owners. A July 2009 market sale of a Class AA office property in the Beltline (Stampede Station) was detailed as was an April 2011 sale of a partial interest in a Class A downtown office (Scotia Centre). The Respondent argued that these transfers and transactions, although not truly comparable market sales data, tended to support the assessment rate. Prices from the transfers/transactions ranged from $313 to $446 per square foot of building area. It was argued that in the absence of open market sales transactions, these indicators were better than nothing.

The subject property, with 19% of its floor area developed for retail uses that achieve very high retail rents (double or triple those for office space) also has minimal vacancy. Investors would recognize the lower investment risk due to these factors and would base a purchase price on a lower than typical capitalization rate. This property and those others on the Mall with substantial retail area are unique properties. The Complainant has provided no evidence to the contrary.

Board's Decision in Respect of Each Issue:

The Board confirms the 2011 assessment of $363,130,000.

Reasons for the Decision:

1. Office rental rate

Office space in Canada Trust Tower is assessed using a typical rental rate of $30.00 per square foot. Respondent support for that rate comes from 16 lease transactions in other AA properties. All leases had commencement dates in the first six months of 2010. The mean, median and weighted mean averages from these 16 leases were $30.84, $32.00 and $32.45 per square foot, respectively.

Eleven lease deals were provided by the Complainant to support the requested $27.00 per square foot office rental rate. Many of these lease deals were included in the data provided by the Respondent. The Complainant relied on the "deal done date (lease close date)" as well as the lease commencement date. Lease close dates ranged from July 2009 to April 2010 and all but one of the lease commencement dates were within the first six months of 2010. The weighted mean rental rate of these 11 lease deals was $27.00 per square foot. For lease areas greater than 10,000 square feet, the weighted mean was $26.67 per square foot.

There is no contention on the part of the Complainant that the subject property is inferior to other downtown Class AA office properties. The rent study that resulted in a market rental rate conclusion of $27.00 per square foot for offices would therefore be applicable to all similar Class AA offices in the same market area. Those other properties are currently assessed using a $30.00 per square foot office rental rate and a 7.0% capitalization rate. It must be assumed that the 7.0% capitalization rate was derived by a process similar to that used to calculate assessments and that the capitalization rates derived from sales were based on AA office space being rented at a market rate of $30.00 per square foot.

There was no capitalization rate study conducted by the Complainant to show that the AA capitalization rate would remain at 7.0% with a different rent rate applied to office space. One of the reasons for this is that there have been no recent sales of Class AA downtown office properties.

The Board finds that the $30.00 per square foot office rent rate applied to the subject is a reasonable rate. While some of the Complainant's comparables suggested that a lower rate might be appropriate for Class AA office space in downtown, there was no reference made to the other input factors such as the capitalization rate. The Board recognizes that the lack of sales makes such an analysis difficult if not impossible, however, the provision of lease data for typical Class AA properties is insufficient to warrant any change without some reasonable consideration about all of the inputs into the income approach formula.

2. Retail space allocation

A copy of a part of a rent roll is insufficient evidence to compel the Board to change the floor areas used by the assessor. An analysis of the Complainant's retail floor area summary versus the amount assessed indicates a variance of 7,003 square feet of space. There is no explanation for this variance. The Board cannot determine from the evidence whether some or all of that space should be allocated to some other space category (i.e. storage).

There are opportunities for the parties to discuss differences of floor areas outside of the CARB environment. It should not be a matter for the Board to deal with unless it is apparent that a significant error has been made.

3. Capitalization rate

There was no market evidence before the Board to support either capitalization rate (6.75% or 7.0%). Both parties provided argument and some evidentiary documentation.

The Respondent puts the subject property into a sub-class of properties that front onto the Stephen Avenue (8 Avenue) Mall and that contain higher than typical amounts of retail space. The Respondent offers that there are five or six properties in this sub-class. All of those properties are assessed using a capitalization rate that is 0.25% lower than the rates applied to other properties in the AA, A or B classes.

The Respondent's evidence brief (Exhibit R1) contains the following explanation of capitalization rate derivation:

> *". . . in the determination of capitalization rates for assessment valuation, it is imperative that the sales analysis process includes not only timely (base year) sales of truly similar properties, but also an analysis predicated on the same Net Operating Income parameters as applied in the NOI that is to be capitalized; That is to say, based on typical market factors, rather than "actual" or historical contract rents, vacancies, operating costs, etc. In this way, Fee Simple market value assessments are achieved."*

It logically follows from the above that the capitalization rate of 7.0%, used in assessing Class AA properties should have been determined from sales of Class AA properties. There were no such sales within the base year. Further, the determination of the 6.5% capitalization rate applied in the subject assessment should have been determined from sales of truly similar properties. There were no such sales within the base year.

The Board does not accept the Respondent's comparison of three totally different properties (downtown Class A, west downtown Class B and suburban Macleod Trail) that sold in 2006 as support for the 0.25% rate adjustment. These properties are vastly different and there is no explanation of how the Scotia Centre property, with a high ratio of retail space, sold at a lower capitalization rate than other Class A properties with typical retail space components.

Both parties provided market reports (Altus Insite, CBRE, Colliers) and argued that the capitalization rate data supported their positions. In a general way, these reports might be useful, however, some analysts do not distinguish between A and AA properties and none of them speak of a sub-class of properties with high ratios of retail floor areas. The Board can draw no conclusions from these reports with respect to the appropriate capitalization rate for application in the assessment of the subject property.

The Complainant's argument regarding the amount of retail space concludes that the subject, with 155,000 square feet of retail cannot be compared to regional shopping centres where there could be 1,000,000 or more square feet. From the floor area perspective, the subject is more closely aligned with smaller power centres or community centres where capitalization rates are 7.25% (higher than the rate for AA offices). Further, it was argued that the amount of net operating income generated by the retail net rentable area is minimal when compared to the overall net operating income as generated by the office, storage and parking areas within the subject property. Office, storage and parking areas generate $20,779,884 in gross income while retail generates $5,667,800 (21.4% of total potential revenue). One fifth of the total is not minimal in the opinion of the Board (recognizing that the net operating income numbers would be different but the ratios would not be significantly different). The Board fails to see how the amount of retail space between the subject, regional shopping centres and power/community shopping centres impacts substantially on capitalization rates. Capitalization rates relate to the quality of income and market risks associated with a property's ability to produce income over a period of time. Size alone is not considered to impact significantly on a capitalization rate.

The Respondent, as a part of its argument that the total assessment must be confirmed by market evidence, has provided data on a number of property transfers (REITs), one 2009 Beltline sale and one 2011 downtown office property sale and concluded that the price per square foot of building area from these transfers (AA @ $446, AA @ $444, A @ $376 and AA @ $436) supports the current $470 per square foot assessment on the subject. The Board does not accept this argument. None of these are sales of truly comparable properties to the subject. If there are no comparable property sales, then there is no data that can be used in a comparison of sales to assessments. The fact that per square foot rates from sales or transfers of non-comparable properties are similar to the unit assessment rate is irrelevant. There is no reliable market evidence that might indicate whether the final assessment is reasonable or unreasonable. For this reason, the test of reasonableness can only be found in analysis of the input factors into the income approach formula.

In conclusion, the Board finds that some of the Complainant's argument relating to the subject's fit within the AA class may have merit however without some type of market evidence to support the argument, there is no compulsion to alter the capitalization rate that has been applied in the subject property assessment calculation.

The 2011 assessment of 751 – 3 Street SW, Calgary is confirmed at $363,130,000.

DATED AT THE CITY OF CALGARY THIS 11th **DAY OF** August **2011.**

W. Kipp

W. Kipp
Presiding Officer

APPENDIX "A"

DOCUMENTS PRESENTED AT THE HEARING AND CONSIDERED BY THE BOARD:

NO.	ITEM
1. C1	Complainant Disclosure
2. R1	Respondent Disclosure

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.