CALGARY
ASSESSMENT REVIEW BOARD
DECISION WITH REASONS

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

between:

Altus Group Limited (representing: 970742 Alberta Limited), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

Mr. J. Krysa, PRESIDING OFFICER
Mr. R. Deschaine, MEMBER
Mr. I. Fraser, 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 Property Assessment Roll as follows:

ROLL NUMBER / BID:	**072033905**
LOCATION ADDRESS:	**4710 17 AV SE**
FILE NUMBER:	**68009**
ASSESSMENT:	**$8,630,000**

This complaint was heard on the 26th day of September, 2012 at the office of the Assessment Review Board located at 4th Floor, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 9.

Appeared on behalf of the Complainant:

- *Mr. K. Fong* *Agent, Altus Group Limited*

Appeared on behalf of the Respondent:

- *Mr. R. Farkas* *Assessor, City of Calgary*

I. Fraser writing for the majority.

Premises Description:

[1] The subject property is located at 4710 17 AV SE known as ***'Forest Lawn Plaza'*** in the southeast community of Forest Lawn and considered to be a neighbourhood shopping centre. The subject property 2012 assessment has been, in part, based on the subject property as having 49,611 square feet of total rentable space within 3 buildings sited on a parcel size of 4.86 acres. The subject property was constructed in 1974 (45,788 square feet) with an additional 3,832 square feet constructed in 1991. The 2012 property assessment as determined by the income approach is $8,630,000.

Issue:

[2] In Section 4 of the Complaint Form the Complainant checked Boxes 3 and 4. At the hearing the Complainant abandoned any argument relating to Box 4. Box 3 indicates the assessment to be the matter of complaint. Attached to the Complaint Form the Complainant identified several grounds for appeal but at the hearing the only issue addressed by the Complainant is summarized in point 5(a):

> *5(a) The assessed capitalization rate is incorrect and should be increased to **8.00 %**.*

[3] At the hearing the Complainant revised the requested capitalization rate of 8.00% to 7.75% providing for a requested assessment of $8,080,000.

Position of the Complainant:

[4] The Complainant does not challenge the following variables:

- the income approach to valuation method as applied to determine the subject 2012 property assessment; nor,
- the assessed area; nor,
- the assessed rental rates; nor,
- the assessed vacancy allowance; nor,
- the associated operating cost allowance; nor,
- the assessed non-recoverable expense allowance.

The Complainant does challenge the assessed capitalization rate of 7.25% and requests the capitalization rate be increased to 7.75%.

[5] In support of the requested capitalization rate (7.75%) the Complainant presented 2 methods of calculating the capitalization rate as summarized on page 100, Exhibit C-1. The 2 methods vary in the manner by which the Potential Gross Income (PGI) is calculated:

Method 1: determines the PGI by applying the ***"assessed income"*** as prepared by the assessor.

Method 2: determines the PGI by applying the ***"typical market income"*** as derived from the rent roll of the specific property which sold and further supplemented by more current market rents to replace older leases within each property.

The PGI is further adjusted for common elements as: vacancy allowances and associated operating cost allowance and non-recoverable expense allowance, to arrive at the Net Operating Income (NOI) for each property which sold. The NOI is then capitalized by the application of a capitalization rate.

Table 1: Method 1 - *"assessed income"* (Summarized from P.100, C-1)

Index	Address	Sale Date (D/M/Y)	Sale Price	Method 1 *"assessed income"*	
				Assessed 'NOI'	**Cap'n Rate**
1	Pacific Place Mall	27-05-2011	$44,000,000	$3,078,515	7.00%
2	Sunridge Sears Centre	19-01-2011	$12,600,000	$825,181	6.55%
3	Calgary East Retail Centre	18-12-2009	$19,585,500	$1,740,874	8.89%
4	Braeside Shopping Centre	14-12-2009	$15,275,000	$1,276,862	8.36%
5	Cranston Market	28-10-2009	$32,000,000	$2,041,265	6.38%
6	McKnight Village Mall	01-05-2009	$19,270,000	$1,590,480	8.25%
7	Chinook Station Office Depot	20-01-2009	$6,930,517	$580,084	8.37%
				Average	**7.69%**

(Intentionally left blank to maintain continuity of schedule following)

Table 2: Method 2 - "*typical market income*" (Summarized from P.100, C-1)

Index	Address	Sale Date (D/M/Y)	Sale Price	Method 2 "*typical market income*"	
				Market 'NOI'	**Cap'n Rate**
1	Pacific Place Mall	27-05-2011	$44,000,000	$3,356,317	7.63%
2	Sunridge Sears Centre	19-01-2011	$12,600,000	$932,844	7.40%
3	Calgary East Retail Centre	18-12-2009	$19,585,500	$1,530,441	7.81%
4	Braeside Shopping Centre	14-12-2009	$15,275,000	$1,177,449	7.71%
5	Cranston Market	28-10-2009	$32,000,000	$2,348,706	7.34%
6	McKnight Village Mall	01-05-2009	$19,270,000	$1,546,503	8.03%
7	Chinook Station Office Depot	20-01-2009	$6,944,450	$600,509	8.65%
				Average	**7.80%**

[6] The Complainant, in Exhibit C-2, presented the supporting documentation for each of the sales properties and the source material from which he derived the NOI as summarized in the above Tables 1 and 2.

Position of the Respondent:

[7] In support of the assessed capitalization rate of 7.25% the Respondent identified 6 sales as summarized on page 30, Exhibit R-1, as follows:

Table 3: Sales relied on by Respondent (Summarized from P.30, R-1)

Index	Address	Sale Date (D/M/Y)	Sale Price	"*assessed typical rents*"	
				Typical 'NOI'	**Cap'n Rate**
1	Pacific Place Mall	27-05-2011	$44,000,000	$3,078,516	7.00%
2	Sunridge Sears Centre	19-01-2011	$12,600,000	$825,181	6.55%
3	Calgary East Retail Centre	18-12-2009	$19,585,500	$1,732,868	8.85%
4	Braeside Shopping Centre	14-12-2009	$15,275,000	$1,084,151	7.10%
5	Cranston Market	28-10-2009	$32,000,000	$1,691,434	5.29%
6	McKnight Village Mall	Not used by Respondent			
7	Chinook Station Office Depot	Not used by Respondent			
8	400 & 1200 163 Quarry Park	04-06-2010	$40,637,317	$2,224,082	5.47%
		Average			**6.71%**

[8] The Respondent noted that whereas the simple average of the capitalization rates is 6.71% (amended during the hearing to 6.65% resulting from a minor adjustment to the assessed NOI relating to index 5) whereas the assessed capitalization rate is 7.25%, which he considered to be

generous.

[9] The Respondent compared the assessments as determined by applying the assessed capitalization rate of 7.25% or alternatively the assessments as would be determined by applying a 7.75% capitalization rate against a time-adjusted sale price for each of the 6 sales, the results of the assessed 7.25% provide for a superior result, that is, an assessment-to-sales ratio closer to 1.00 as summarized on the following Table 4.

Table 4: Comparative 'ASR' Analysis

Index	Address	Sale Date (D/M/Y)	Time-adjusted Sale Price	Comparative Analysis			
				Assessment @7.25%	**ASR**	**Assessment @7.75%**	**ASR**
1	Pacific Place Mall	27-05-2011	$43,952,585	$42,460,000	0.97	$39,720,000	0.90
2	Sunridge Sears Centre	19-01-2011	$12,589,384	$11,380,000	0.90	$10,640,000	0.85
3	Calgary East Retail Centre	18-12-2009	$20,302,132	$22,430,000	1.10	$21,000,000	1.03
4	Braeside Shopping Centre	14-12-2009	$15,932,211	$15,150,000	0.95	$14,180,000	0.89
5	Cranston Market	28-10-2009	$33,582,739	$28,580,000	0.85	$26,740,000	0.80
8	400 & 1200 163 Quarry Park	04-06-2010	$41,339,687	$31,270,000	0.76	$29,250,000	0.71
	Simple Average				**0.92**		**0.86**

Majority Decision:

[10] The nub of the issue before the Board in the current appeal centers on the derivation of the appropriate capitalization rate derived from properties which had sold in the marketplace. The sale price is a fixed denominator in the equation where the capitalization rate is determined by dividing the Net Operating Income (NOI), the numerator, by the sale price (NOI / Sale Price). The disagreement between the parties is not, of course, over the sale price of those properties which sold but rather the disagreement rests in the determination of the Potential Gross Income (PGI) as adjusted to arrive at the NOI. A change to any factor (rent rates, vacancy rates, and other expenses) leading to the resultant NOI will impact the determination of the capitalization rate.

[11] Whereas the Complainant presented extensive materials relating to the derivation of the PGI associated with each sale property as reported in Tables 1 and 2 based on the calculations reported in Exhibit C-2, the Complainant presented not a shred of evidence to support the subject assessed income which he did not challenge. As noted, the PGI is an integral component not only for the determination of the appropriate NOI but also the determination of the subsequent assessment (NOI / Capitalization rate). The Board considers that a challenge to the correctness of the capitalization rate necessarily requires a verification of the subject PGI and that both NOI and capitalization rate are to be determined using the same assumptions to be mathematically correct (see ***Westcoast*** following para. 14).

[12] The Complainant, in deriving the "typical market income" as reported in Table 2 (method 2)

has relied, in the main, on the site specific rent rolls for each reported sale property. In other words, the derived income is site specific, with adjustments to the rent to update site specific stale-dated leases with more current market rents, and at the time of sale. For example, the sales reported as having occurred in 2009 have their respective NOI determined based on the calculated income derived in 2009 and used in the 2010 assessment year having a date of assessment as at July 1, 2009. In a similar manner the 2010 sales applied 2010 site specific leases as adjusted for stale-dated site specific leases and the 2011 sales applied 2011 leases as adjusted for stale-dated site specific leases.

[13] For mass appraisal purposes the Board finds this method (Method 2) to be in violation of the assessment requirements as set out in s.1(k) of ***Alberta Regulation 220/2004, Matters Relating to Assessment and Taxation Regulation***:

> (k) "mass appraisal" means the process of preparing assessments <u>for a group of properties using standard methods and common data</u> and allowing for statistical testing;
>
> (Emphasis added.)

[14] Further, the Board sought guidance from the courts. In ***Westcoast Transmission Limited v. Assessor of Area 9 – Vancouver*** (1987), Stated Cases, Case 235, [1987] B.C.J. No. 1273 (S.C.). Mr. Justice Cumming, confronted with exactly the same issue as currently before this Board, stated under the heading "The Assessment Process":

> "It is common ground that the income approach is an appropriate and, except in unusual circumstances, the most appropriate method of assessing the actual value of commercial property such as that under consideration here.
>
> "It will perhaps remove some of the mystique in the assessment process to lay out the principles applicable to this method of valuation. I take them, with some minor editorializing on my part, from the written submission filed by Mr. Greenwood. There are various approaches to an income valuation. A standard one is known as the capitalization approach. This approach is really a form of the "market approach". Statistics are gathered on the sales of buildings which are considered comparable to the subject property from a point of view of quality, amenities, location, and state of repair. The price at which each building sells in the relevant time period is compared with the income reasonably generated by the building. Income divided by sale price generates a factor called the "capitalization rate". The various capitalization rates for comparable buildings are analyzed with a view to developing a "typical" capitalization rate for that class of property.
>
> "The subject building, (which one assumes has not itself sold in the time frame under consideration), can then have its value estimated on the assumption that it also would

sell at the same capitalization rate as have others. The appraiser therefore estimates the income generated by the subject building, and divides it by the typical capitalization rate to derive an estimate of value.

"For this process to work, it is evident that the appraiser must make some choices about the concepts to be used, and then to use them consistently. "Income", for example, can mean a number of different things. It may mean a gross or a net income, or a "triple net" income. The appraiser normally will select a net income, recognizing a standard list of expenses to be deducted from the gross.

"The appraiser could also use an actual net income, or a calculated income generated on certain standard expectations about the use of the building over time. Actual incomes from any building will vary over short time frames, as tenants move in and out, or as unusual expenses occur. Buildings are not typically bought for short time frames, and thus appraisers attempt to deduce what the typical income would be over a long term (in current dollars), before they calculate a capitalization rate from any sale. They call this, variously, a stabilized net income, or an economic net income, as opposed to an actual net income at the snapshot date of valuation.

"Actual incomes are also affected by the abilities of the management of the day. A better manager might reduce expenses, or raise rents successfully, and realize a greater return from the building. When estimating what a building would sell for to a new owner and manager, the qualities of the existing management are eliminated from the analysis.

"in valuation theory, the value of an income producing property is merely the present value of future expected income to be generated by the property. The future being looked at is the long term future, and when the appraiser capitalizes an existing or present income, he does so on the premise that the figure being capitalized is representative (in current dollars) of the long term stabilized situation, not of some short term situation. Appraisers explain this by saying that they are "capitalizing the income in perpetuity".

"For these various reasons, economic net incomes are universally used by appraisers in arriving at a capitalization rate for the building which has sold. This is so even though there are occasions when an appraiser testifies that the actual net income should be used, because it is the best estimate in fact of the economic income of the particular property.

"I stated above that the concepts used, in developing capitalization rates for application to the subject, should be used consistently. Thus it makes no sense to develop a capitalization rate on one set of assumptions about long-term vacancy rates, long-term rents, and long-term expenses, and then apply that rate to the income of the subject property that is not derived in the same way.

"The choice of a vacancy rate goes directly into the calculation of gross income, from which the appraiser then deducts expenses to arrive at an estimate of net income. All of these factors, for consistency, should be used in the same manner as they were used in the study of comparables which resulted in the development of the capitalization rate. To do otherwise is to offend appraisal theory, and is likely to produce a mistaken result."

(Emphasis added.)

[15] The Board reviewed the Complainant's submission and notes that 5 of the sales relied on by the Complainant occurred in 2009 (see Tables 1 and 2, Indices 3 through 7). Those sales may have had relevance for the 2010 assessment year (valuation date as of July 1, 2009) but without adjustments for time, or confirmation that no adjustments were warranted, those 5 sales, now 2 years later, lack relevance for the 2012 assessment having a valuation date as of July 1, 2011. Accordingly, the Board gave no weight to these sales. The Board notes that these 5 sales, for their respective 2010 assessments had incorporated a capitalization rate of either 8.00% or 8.25% as follows:

Table 5: 2010 Assessed Capitalization Rate

Index	Address	Name	2010 Assessed Capitalization Rate
3	2929 Sunridge Way NE	Calgary East Retail Centre	**8.00%** (p.48, C-2)
4	1919 Southland Drive SW	Braeside Shopping Centre	**8.25%** (p.53, C-2)
5	356 Cranston Road SE	Cranston Market	**8.00%** (p.76, C-2)
6	5220 Falsbridge Gate NE	McKnight Village Mall	**8.00%** (p.86, C-2)
7	306 Glenmore Trail SW	Chinook Station Office Depot	**8.00%** (p.92, C-2)

[16] The Respondent presented time adjustments for the sale properties as shown in Table 4. The Complainant critiqued the time-adjustment factors as determined by the Respondent sufficiently such that the Board had no comfort in accepting the time-adjustments and disregarded the reported time-adjusted values shown on Table 4.

[17] The Board has previously disregarded the 2009 sales as not having been shown to have current relevance. The Board accepts that the 2011 sales would require no time adjustments and are relevant within the time frame under review. The following Assessment-to-Sales ratio analysis indicates that the assessed capitalization rate of 7.25% provides for a superior result compared to the requested capitalization rate of 7.75%. Further, the Board agrees with the Respondent that the assessed rate of 7.25% appears generous based on the following analysis.

Table 6: Comparative 'ASR' Analysis (Unadjusted Sale Price)

Index	Address	Sale Date (D/M/Y)	Unadjusted Sale Price	Comparative Analysis			
				Assessment @7.25%	**ASR**	**Assessment @7.75%**	**ASR**
1	Pacific Place Mall	27-05-2011	$44,000,000	$42,460,000	0.97	$39,720,000	0.90
2	Sunridge Sears Centre	19-01-2011	$12,600,000	$11,380,000	0.90	$10,640,000	0.84
				Simple Average	**0.94**		**0.87**

[18] For all of the above reasons the Board does not find the requested capitalization rate of 7.75% to be mathematically correct for the preparation of assessments nor would 7.75% yield a superior ASR result as indicated in Table 6.

[19] The assessment of $8,630,000 is confirmed.

DATED AT THE CITY OF CALGARY THIS 13 **DAY OF** November **2012.**

I. Fraser, Panel Member

Agreed: "R. Deschaine", Panel Member

Dissenting Opinion: J. Krysa, Presiding Officer:

[20] I respectfully disagree with the majority decision of my colleagues as set out above for the following reasons:

[21] I find the Complainant's "Capitalization Rate Method 2" analysis is compelling evidence of typical market capitalization rates. The analysis is well supported with documentary evidence of the properties' rent rolls and ARFI (Assessment Request For Information) responses, and is consistent with well established appraisal theory and the AAAVG (Alberta Assessor's Association Valuation Guide). In my view, the methodology mirrors the motivations of participants in the marketplace and therefore, demonstrates valid indications of market capitalization rates.

[22] Although the Respondent presented argument in respect of the Complainant's analysis and methodology, the Respondent failed to provide any relevant market evidence to refute the Complainant's market rent inputs, analysis and capitalization rate conclusion. In light of the above, I believe the Complainant has clearly presented sufficient evidence to establish a *prima facie* case, and the evidentiary burden is properly shifted to the Respondent.

[23] In contrast, I find that the Respondent's capitalization rate analysis (based on assessed income) was not supported with any documentary evidence to demonstrate that the assessed rent coefficients are reflective of the "typical" market rents each of the properties are able to achieve. On the contrary, the Complainant's rent roll and ARFI evidence in respect of the sales clearly demonstrates that the Respondent's "assessed" rent rates assigned to several of the lease spaces are well below the levels exhibited by leasing activity near the sale date, resulting in significantly underestimated net operating incomes and consequently, inaccurate capitalization rate conclusions. The table below, in respect of the bank premises at Cranston Market, sets out but one example of the significant discrepancy between the Respondent's "assessed" rents (as a proxy for "typical" market rent) used to derive the capitalization rate, and the "market" rents a purchaser or vendor would base a real estate transaction on.

	Effective Date	"Market" Rent Rate	Source
Sale	Oct 28, 2009		R1, p.30
Lease Rent Rate	Nov17, 2009	$55.00	C2, p.154
*Assessed Rent	Jul 01, 2009	$28.00	R1, p.31

[24] Although the sale price and corresponding "market" capitalization rate of the property would reflect the $55.00 per sq.ft. market rent rate exhibited by the lease signed within 3 weeks of the sale date, the Respondent's capitalization rate calculation in respect of these premises, founded on a $28.00 per sq.ft. assessed rent would suggest a capitalization rate approximately one half of the "market" rate exhibited by the sale. The Complainant's evidence further illustrates that the Respondent's methodology is problematic, when the capitalization rate conclusion from the Respondent's analysis is applied to value the same space in 2011 with an assessed "typical" market rent rate of $43.00 per sq.ft. (effective July 01, 2010) [*C2, p.79*]; and in 2012 with an assessed "typical" market rent rate of $45.00 per sq.ft. (effective July 01, 2011) [*C3, p.200*]. I also note that the "allowances" in respect of vacancy rates and operating costs applied in the preparation of assessments in subsequent years, are inconsistent with the allowances employed in the derivation of the capitalization rates, contrary to the principles set out in ***Westcoast Transmission Limited v. Assessor of Area 9 – Vancouver*** (1987), Stated Cases, Case 235, [1987] B.C.J. No. 1273 (S.C.).

[25] Further, I find the Respondent's 7.25% capitalization rate conclusion is arbitrary and without market support. The Respondent's own analysis establishes a median capitalization rate of 6.77%, and there was no market evidence provided to quantify the +0.5% adjustment for the two sales (Quarry Park and Cranston Market) that the Respondent concedes are "suspect" due to their 5.47% and 5.29% capitalization rates. Also, the Respondent conceded that the assessed $18.00 per sq.ft. rent coefficient applied to the Cranston Market anchor space is not the "typical" rate, and should be $15.00 per sq.ft., resulting in a revised capitalization rate from 5.29% to 4.9% for this sale.

[26] I find the Respondent's wide range of indicated capitalization rates, from 4.9% (corrected) to 8.85%, is not compelling evidence that supports the Respondent's "typical" 7.25% capitalization rate conclusion; whereas only two of the Respondent's six sales exhibit capitalization rates within a +/- 0.50% margin (6.75% to 7.75%) of the Respondent's "typical" capitalization rate conclusion.

[27] I believe that the Complainant's "Method 2" analysis fully complies with the mass appraisal provisions of the legislation, as the definition of mass appraisal indicates that assessments for a group of properties are to be "prepared" using standard methods and common data and allowing for statistical testing. In my view, the Complainant's "typical" 7.75% capitalization rate conclusion is valid "common data" that can, and should be applied in the preparation of neighbourhood shopping centre assessments.

[28] Further, I accept that the Complainant's 2009 sales are relevant market indicators in respect of a July 1, 2011 valuation date, and note that both parties included 2009 sales in their capitalization rate analyses. Moreover, the Respondent raised no objection to the Complainant's three, late 2009 sales that occurred within twenty months of the valuation date.

[29] In my view, it is unnecessary for the Complainant to be compelled to verify the subject's current assessed income, as neither party provided any evidence or argument to suggest that it is in some way inaccurate. Moreover, if the Complainant's proposed current assessed income is inappropriate in some way, (which neither party suggests it is), I believe it is the Respondent's responsibility to provide evidence to refute the Complainant's application of the capitalization rate, and in this instance, the Respondent failed to do so.

[30] In light of all of the above, and whereas the Board finds that the Respondent's ASR (Assessment to Sale Ratio) analysis is inaccurate and irrelevant, it is my opinion that the Respondent failed to provide sufficient evidence to meet the evidentiary burden, and demonstrate that the assessment is correct.

EXHIBITS RECEIVED AT HEARING

Exhibit C-1: Complainant's Disclosure
Exhibit C-2: Complainant's Disclosure
Exhibit R-1: Respondent's 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.*

Subject	Property Type	Property Sub Type	Issue	Sub-Issue
CARB	Retail	Neighbourhood Shopping	Income Approach	Capitalization Rate