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:

Anthem Heritage Hill Ltd. (as represented by Altus Group), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

W. Kipp, PRESIDING OFFICER
R Cochrane, MEMBER
D. Steele, 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: **112 136 007**

LOCATION ADDRESS: **8180 Macleod Trail SE, Calgary AB**

HEARING NUMBER: **63370**

ASSESSMENT: **$41,100,000**

This complaint was heard on the 11th, 12th and 13th days of October, 2011 at the office of the Assessment Review Board located at Floor No. 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 4.

Appeared on behalf of the Complainant:

- *A. Izard & K. Fong (Altus Group)*

Appeared on behalf of the Respondent:

- *R. Ford & H. Yau (Assessment Business Unit)*

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

One of the issues in this complaint was the capitalization rate to be used in the application of the income approach. The Complainant prepared a "Capitalization Rate Study." That study pertained to this file plus five other files (#63984, #63985, #64188, #63939, #64023) that were to be heard as part of the agenda for the week. It was agreed by the parties and accepted by the Board that the Complainant would present the capitalization rate evidence just once and that it would be carried forward to the other hearings where the capitalization rate is an issue. The Respondent incorporated its capitalization rate analysis and rebuttal into the disclosure brief for each file but chose to address that issue just once and then carry forward all evidence and argument to the other affected hearings. The Complainant agreed and the Board accepted this proposal. The Complainant's rebuttal to the Respondent's capitalization rate analysis was provided in three parts that were marked as Exhibits C2A, C2B and C3. One copy of those submissions was provided to the Board and they will be retained in File 63984. The evidence and argument regarding capitalization rate was heard on October 11 and 12, 2010.

The Respondent objected to the admission of the Complainant's rebuttal evidence on the ground that it was different than rebuttal evidence disclosed in other hearings. The Complainant argued that it was essentially the same material and that it had been properly disclosed within the timelines prescribed by the regulations. The rebuttal document comprising 535 pages was filed in three parts and given its size, the Board's initial decision was to postpone any objections until the point in the hearing where the Complainant addressed that evidence. At that point in the hearing, the Respondent again raised some objections as the rebuttal evidence was being presented. The Board found that the rebuttal disclosure had been in accordance with the requirements of the regulations, none of the material was new evidence and none of it was unrelated to the issue. The decision of the Board was to admit the entire rebuttal evidence package.

Property Description:

The property that is the subject of this complaint is a community shopping centre known as Heritage Hill Plaza. The property has a Macleod Trail address but the primary access is from Flint Road SE which passes by the easterly property line. On the 9.13 acre site are two buildings. The larger building is a retail centre containing 128,871 square feet. The second building is a 43,192 square foot four level office building with some retail occupancies on the lower floor. The year of construction for both buildings is 1972.

The 2011 assessment of $41,100,000 was determined by the income approach. Rental rates from $12.00 to $25.00 were assigned to various retail occupancies and $25.00 was set for office space. One junior big box store (Winners) is reduced by 1.0% for potential vacancy losses while all other occupancies are given a 4.0% vacancy allowance. Typical operating costs are $7.00 per square foot for the property and a 1.0% non-recoverable expense allowance is made. The resulting net operating income amount of $2,980,000 is converted by a 7.25% capitalization rate to the $41,100,000 assessment ($238.87 per square foot of rentable area).

Issues:

The Assessment Review Board Complaint form filed March 4, 2011 had check marks in boxes No. 3 (Assessment amount) and No. 4 (Assessment class) in Section 4 (Complaint Information). For Section 5 (Reason(s) for Complaint), an attachment to the form listed 17 grounds for appeal.

At the hearing, the Complainant argued three issues:

Issue 1: Should the capitalization rate be increased from 7.25% to 7.75%?

Issue 2: Should the following rental rates be reduced: office space from $25.00 to $15.00 or $19.00 per square foot; the junior big box space from $17.00 to $14.00; and, the retail space over 6,000 square feet from $16.00 to $15.00 per square foot?

Issue 3: Should the vacancy rate be increased for the retail building?

Complainant's Requested Value: $23,880,000 if office space rent rate is $15.00
$24,640,000 if office space rent rate is $19.00

Party Positions on the Issues:

Complainant's Position:

Issue 1: Should the capitalization rate be increased from 7.25% to 7.75%?

The subject property and others in its class are assessed by the Respondent using the income approach with the capitalization rate set at 7.25%. A "*Community-Neighbourhood Shopping Centres: 2011 Capitalization Rate Analysis*" conducted by Altus Group (Altus Cap. Rate Study) is based on shopping centre sales that occurred in January 2009 or later and it concludes that the correct capitalization rate for this group of properties is 7.75%.

The Complainant cites numerous court and assessment tribunal decisions as well as appraisal textbooks and Alberta Government and Alberta Assessors Association materials that support the practice of deriving capitalization rates using actual income and actual sale price for each property being analyzed in a capitalization rate study. Further, the evidence contains materials produced by the City of Calgary in years past that described this extraction method as being the most appropriate method. That is generally the procedure used in the Altus Cap. Rate Study wherein two capitalization rates are derived from sales – one based on "typical" income and one based on "market" income. In the study, it was found that there was not a wide discrepancy in the rates from the two derivation methods utilized (typical or market rental income).

One of the documents presented by the Complainant is from the Alberta Assessors' Association Valuation Guide setting out valuation parameters for the assessment of income producing properties. On the issue of determining base rent, the following portion of the guide is highlighted:

Base Rent

To determine the current market rent for each tenant, the following guidelines are provided (in order of descending importance):

1. *For most tenants the best source of market rent information is the rent roll. Using these rent rolls, the best evidence of "market" rents are (in order of descending importance):*
- *Actual leases signed on or around the valuation date.*
- *Actual leases within the first three years of their term as of the valuation date.*
- *Current rents for similar types of stores in the same shopping centre.*
- *Older leases with active overage rent or step-up clauses.*
2. *As a secondary source of rent information, and as a check on the rents derived from the actual rent rolls, the rental rates can be compared to the rents established for similar tenants in other similar properties.*
3. *If comparable information is not available, it may be necessary to analyze the existing leases and interview the owner and tenant(s) to determine what the current rent on the space should be.*

Altus followed these guidelines in its analysis of each shopping centre in its study. Five sale transactions were examined using typical parameters for vacancy, operating costs and non-recoverable expense (these are the typical parameters used by the Respondent in making assessments for this class of shopping centre). Results are summarized below:

PROPERTY:	**2929 Sunridge Way NE**	**1919 Southland Drive SW**	**356 Cranston Road SE**	**5220 Falconridge Gate NE**	**306 Glenmore Trail SW**
Sale Date	18-Dec-09	14-Dec-09	28-Oct-09	01-May-09	20-Jan-09
Sale Price	$19,585,500	$15,275,000	$32,000,000	$19,270,000	$6,944,450
Typical PGI	$ 1,578,842	$ 1,216,777	$ 2,454,272	$ 1,602,643	$ 624,162
Typical NOI	$ 1,530,441	$ 1,177,450	$ 2,348,706	$ 1,546,503	$ 600,509
CAP. RATE	7.81%	7.71%	7.34%	8.03%	8.65%
Mean Cap.			**7.91%**		
Wt. Mean Cap.			**7.74%**		
Market PGI	$ 1,523,063	$ 1,182,856	$ 2,458,470	$ 1,657,182	$ 625,000
Market NOI	$ 1,475,770	$ 1,144,540	$ 2,352,717	$ 1,600,847	$ 601,322
CAP. RATE	7.54%	7.49%	7.35%	8.31%	8.66%
Mean Cap.			**7.87%**		
Wt. Mean Cap.			**7.71%**		

Legend: PGI = Potential Gross Income; NOI = Net Operating Income;
CAP. RATE = Capitalization Rate; Wt. Mean Cap. = Weighted Mean Capitalization Rate

Rents were obtained from actual leases in place at the time of sale and from new leases in similar shopping centres within the market area of each property.

Issue 2: Should the following rental rates be reduced: office space from $25.00 to $15.00 or $19.00 per square foot; the junior big box space from $17.00 to $14.00; and, the retail space over 6,000 square feet from $16.00 to $15.00 per square foot?

The Complainant argues that the Respondent has incorrectly classed the subject office building as a Class A2 building whereas it should be as low as Class C. Assessments of newer offices in better locations have rent rates of $15.00 to $20.00 per square foot applied to office space.

In the retail building, a December 2010 rent roll shows some current leasing. A December 1, 2010 lease of 7,197 square feet for an auto parts store specifies a rent rate of $11.00 per square foot. An October 2010 lease of 9,376 square feet has a gross rent rate equivalent to $12.80 per square foot. After allowing for operating expenses, the net rate is under $10.00. Even a January 2007 lease of 6,030 square feet only has a rent rate of $15.00 per square foot and the market was significantly stronger at that time. An October 2006 lease of 10,913 square feet specifies a $15.00 rent rate as well.

A rent roll for the office building showed eight leases with 2009 or 2010 lease starts. Rent rates range from $12.00 to $22.00 per square foot. The mean average rate is $15.00 and the weighted mean is $13.93 per square foot.

A survey of market rents indicates median and mean average rates of $11.90 to $14.60 per square foot for larger rental unit spaces and $14.00 to $15.34 per square foot for junior big box stores.

The market and assessment data shows that the subject office space should be assigned a rent rate of $15.00 per square foot or at the very most, $19.00 per square foot. The Winners store (junior big box) in the retail section should have a rent rate of $14.00 per square foot and spaces over 6,000 square feet in area should have a $15.00 per square foot rate.

Issue 3: Should the vacancy rate be increased for the retail building?

In 2008, a large space tenant (House of Tools) went into receivership and closed its business in the retail centre. The December 2010 rent roll for the retail building shows four vacant tenant areas with a total area of 37,274 square feet (28.99% of total area). The vacancy rate had been around the same level through 2010. The subject property history indicates to the Complainant that the vacancy allowance for assessment purposes should be 30% for the whole retail building except for the junior big box store which should remain at 1.0%.

Respondent's Position:

Issue 1: Should the capitalization rate be increased from 7.25% to 7.75%?

The Respondent argued that consistency demands that capitalization rates be derived in similar fashion to the way in which they are applied in valuing a property. That is that typical factors, including rents must be applied to a property when analyzing its sale. The analyst must be careful to apply those typical rates and factors that were applicable as at the time of the sale.

The Respondent analyzed eight shopping centre transactions to obtain the 7.25% capitalization rate that is applied to community-neighbourhood shopping centres in making their assessments:

Address	Sale Date	Sale Price	Typical PGI	Typical NOI	Typical Cap.	Actual Cap.
1221 Canyon Meadows Drive SE	14-Aug-08	$31,500,000	$2,150,233	$2,048,692	6.50%	5.82%
306 Glenmore Trail SW	20-Jan-09	$ 6,944,450	$ 594,440	$ 580,084	8.35%	8.79%
873 – 85 Street SW	16-Mar-09	$23,500,000	$1,549,942	$1,493,781	6.36%	6.77%
5220 Falconridge Drive NE	19-May-09	$19,270,000	$1,652,396	$1,590,481	8.25%	7.87%
356 Cranston Road SE	28-Oct-09	$32,000,000	$2,201,005	$2,041,266	6.38%	7.14%
1919 Southland Drive SW	14-Dec-09	$15,275,000	$1,324,081	$1,157,940	7.58%	6.49%
2929 Sunridge Way NE	18-Dec-09	$19,585,500	$1,739,085	$1,640,846	8.38%	7.34%
400 & 1200, 163 Quarry Park Bv SE	06-Apr-10	$40,637,317	$2,195,977	$2,035,727	5.01%	5.94%
Median Cap. Rate					7.04%	6.95%
Average Cap. Rate					7.10%	7.02%

Legend: PGI = Potential Gross Income; NOI = Net Operating Income;
Cap./Cap. Rate = Capitalization Rate

The Respondent's methodology involves estimating typical income which is income generated by a property using typical market rental rates. Vacant spaces are assumed to be leased up at the typical market rental rates. Five of the sales were also included in the Altus Cap. Rate Study but the calculated capitalization rates differed in every one:

Property	**2929 Sunridge Way NE**	**1919 Southland Drive SW**	**356 Cranston Road SE**	**5220 Falconridge Gate NE**	**306 Glenmore Trail SW**
Complainant Typical Cap.	7.81%	7.71%	7.34%	8.03%	8.65%
Respondent Typical Cap.	8.38%	7.58%	6.38%	8.25%	8.35%

Issue 2: Should the following rental rates be reduced: office space from $25.00 to $15.00 or $19.00 per square foot; the junior big box space from $17.00 to $14.00; and, the retail space over 6,000 square feet from $16.00 to $15.00 per square foot?

Assessments of properties such as the subject are prepared using the income approach wherein rents for various space types are "typical" rents. Actual rents from the subject should not be relied upon exclusively in the valuation.

Tables of rent data are provided to support various rates applied to space in the subject. For larger retail spaces (over 6,000 square feet), business tax assessment rates are from $15.00 to $18.00 per square foot. Lease data for Class A and B junior big box stores in Calgary range from $12.50 to $30.91 and average from $17.15 to $18.26 per square foot. Class C junior big box stores are assessed at $12.00 per square foot.

Comparable shopping centre office space is consistently assessed using a $25.00 per square foot rent rate. An example is Glenmore Landing on 90 Avenue SW.

Issue 3: Should the vacancy rate be increased for the retail building?

The Respondent conducts vacancy studies in order to arrive at typical vacancy levels for various property types. For retail properties such as the subject, the study indicates typical vacancy at 4.0% but at just 1.0% for junior big box stores. The 4.0% rate applies to office space in shopping centres.

While the subject may have had blocks of vacant space from time to time, there is no evidence to show that the property has a chronic vacancy problem. If there was chronic vacancy, the Respondent would recognize that and reflect it in assessments.

Board's Decision:

The 2011 assessment of this property is reduced to $32,490,000.

Reasons for the Decision:

Issue 1: Should the capitalization rate be increased from 7.25% to 7.75%?

The Respondent provides sales summary reports from Realnet and/or Alberta Data Search for each of the eight properties in its study as well as land titles documentation and corporate search returns. In a few cases, a portion of an Assessment Request For Information (ARFI) return is provided. In some cases, copies of disclosure documents filed by Altus Group as part of assessment complaints against those properties are provided along with the argument that Altus had asked for certain rates during their handling of complaints but were applying different rates in analyzing those same properties for capitalization rate derivation.

The Board excludes two of the sales relied upon by the Respondent and takes a cautious approach to a third sale.

The Deer Valley Shopping Centre (1221 Canyon Meadows Drive SE) was sold to an investor who undertook a major redevelopment of the property soon after taking possession. The Respondent provides data to the effect that development permits were not in place at the time of the sale but that is a moot point. The usefulness of this sale depends on the motivations of the parties at the time of the sale. If there was consideration given to land upon which additional retail building could take place then that would probably have brought a higher price than is indicated by analysis of the existing income. Realnet, in reporting the sale, stated that the purchaser intended to demolish a standalone building and redevelop a portion of the property with approximately 60,000 square feet of retail space. Realnet would have received their information from the purchaser or an agent so it is probable that the additional development was recognized by the parties to the transaction and thus, the price would not have been based on existing income alone. In any event, the motivations of the parties are not clear so the sale cannot be relied upon.

The Quarry Park shopping centre (400 & 1200, 163 Quarry Park Boulevard SE) produces a very low capitalization rate in the Respondent's analysis. The net operating income based on the Respondent's typical rents is significantly lower than total rent indicated by the rent roll that is in the Respondent's evidence ($2,035,727 versus +/-$2,700,000). All leases in the property have commencement dates that are contemporaneous with the valuation date so it must be assumed, based on the information provided, that actual rents are similar to market or typical rents. In any event, the details of the sale and property operations are insufficient to provide a meaningful analysis. The very low capitalization rate of 5.01% is so much below the range from other properties that it cannot be given any weight.

The Complainant raises doubt about the West Springs Village (873 – 85 Street SW) sale. There was no broker involvement and there was reportedly some income guarantees made by the vendor. Nevertheless, the Board finds that the sale may have been market driven even though it may not have been thoroughly exposed to the market.

The Respondent provides a table summarizing the capitalization rate derivations from the eight sales that were analyzed. There is no support or explanation of the typical net operating income amounts used in the analysis. Copies of ARFI's and/or rent rolls are in the evidence. However, the total amounts do not match with the typicals used in the analysis. Net operating income is a key component of the capitalization rate derivation formula. The Respondent provides no compelling evidence to support its net operating income estimates for the sale properties in its analysis therefore the Board does not give weight to those capitalization rates.

Braeside Centre (1919 Southland Drive SW) is analyzed using a 9.0% vacancy rate which is a holdover from its former classification as a strip centre. Typical vacancy for southwest quadrant community/neighbourhood shopping centres is 4.0%. The error, which had apparently been discovered some time ago, is not corrected for this hearing. In the capitalization rate analysis, 2010 parameters are used to analyze the Sunridge Centre (2929 Sunridge Way NE) sale and 2009 parameters are used for the analysis of Braeside, yet the two sales occurred just four days apart in December 2009.

An Assessment to Sale Ratio (ASR) analysis in the Respondent's evidence indicates that the median ASR for the five sales in the Complainant's evidence would be 0.97 using a 7.25% capitalization rate and 0.91 using the requested 7.75% capitalization rate. For assessment quality purposes, the ideal range of ASR's is from 0.95 to 1.05. These ASR's are based on time adjusted sales prices for the comparables. There are inconsistencies in the time adjustment rates that the Respondent is unable to explain. For example, Braeside Centre and Sunridge Centre sold just four days apart in December 2009. The Braeside sale price is adjusted upwards by 4.50% while the Sunridge Centre price is adjusted upwards by 3.86%.

The Board finds that the Complainant's capitalization rate study is researched and supported by market evidence. The calculated capitalization rates are credible and they are accepted by the Board as the superior market derived capitalization rates.

The Respondent's evidence comprises a table showing capitalization rate derivations from sales, documentation to support sale prices, copies of market survey reports by Colliers International and CB Richard Ellis and a substantial amount of documentation showing where Altus Group has provided varying information at other complaint hearings for various properties. There is insufficient evidence to directly support the capitalization rate conclusion of 7.25%. The Board gives no weight to the market survey reports because those reports are prepared and published as marketing tools by those real estate brokerages and there is no explanation of how surveys are conducted or how thoroughly they cover the market. The Board does not make its decisions based on discrepancies in evidence or requests on past hearings on other properties. It is the evidence and argument before this current Board that is weighed. The Board has read and considered decisions rendered by prior CARB's but gives them limited weight because it is not clear whether those prior decisions were made on the same evidence as is before this Board.

With the Deer Valley and Quarry Park properties removed from the Respondent's study, the remaining six sales produce median and mean capitalization rates of 7.92% and 7.55%, respectively. These rates support the requested rate of 7.75% more than the 7.25% assessment capitalization rate.

Issue 2: Should the following rental rates be reduced: office space from $25.00 to $15.00 or $19.00 per square foot; the junior big box space from $17.00 to $14.00; and, the retail space over 6,000 square feet from $16.00 to $15.00 per square foot?

From the evidence before the Board, it is clear that Heritage Hill Plaza is not a Class A property. Rent roll data for the office building shows eight leases in the office building with 2009 and 2010 start dates that produce a weighted mean rent rate of $13.93 per square foot. Some of the leases started after the July 1, 2010 valuation date. For the four leases with start dates prior to July 2010, the weighted mean is $14.70 per square foot.

The Board does not accept the argument that office space in Glenmore Landing shopping centre is comparable to that in the subject office building. The office building on the Macleod Trail Co-op shopping centre is assessed using a rent rate of $15.00 per square foot. The Board finds this to be compelling evidence that the subject should reflect a rate of no more than $15.00.

For retail space, actual junior big box store lease rates support an adjustment of the rate for the subject Winners store to $14.00 per square foot. For other commercial rental unit space, the Board is not convinced that the rates of $16.00 to $25.00 per square foot should be changed. From an equity perspective, those rates appear to have been consistently applied to shopping centres in the vicinity of the subject. The Complainant offered that the Macleod Trail Co-op shopping centre is most comparable to the subject as far as office space is concerned. The Board notes that rent rates applied to retail space in that centre are consistent with those applied to the subject.

Issue 3: Should the vacancy rate be increased for the retail building?

There is insufficient evidence to support an argument that the subject property suffers from chronic vacancy. One large block of space was considered to be vacant when the House of Tools went into receivership, however a document in the Complainant's rebuttal shows that the receiver continued to pay rent on that space until at least the middle of 2009.

The Respondent consistently applies typical vacancy rates to various types of space in various types of properties. Vacancy surveys based on reports from property owners and managers form the basis for those rates and the Board accepts them for this assessment.

DATED AT THE CITY OF CALGARY THIS 16th **DAY OF** NOVEMBER **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
3. C2A	Part 1 Complainant Rebuttal
4. C2B	Part 2 Complainant Rebuttal
5. C3	Part 3 Complainant Cap Rate Rebuttal
6. C4	Complainant Rent/Vacancy Rebuttal
7. C5	Colour photos from Ex C1

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.

For Administrative Use:

Appeal Type	Property Type	Property Sub-Type	Issue	Sub-Issue
CARB	Retail	Neighbourhood Mall	Income Approach	Capitalization Rate Rent/Lease rates