Calgary Assessment Review Board

DECISION WITH REASONS
& DISSENTING OPINION

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:

Barclay Square Capital Corp. (as represented by MNP LLP), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

PRESIDING OFFICER: T. Helgeson
BOARD MEMBER: J. Kerrison
BOARD MEMBER: Y. Nesry

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 2013 Assessment Roll as follows:

ROLL NUMBER: 067136002

LOCATION ADDRESS: 1300 8 Street SW

FILE NUMBER: 70519

ASSESSMENT: $9,800,000

This complaint was heard on the 9th of July, 2013 at the office of the Assessment Review Board located at Floor Number 3, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 8.

Appeared on behalf of the Complainant:

- *G. Worsley*

Appeared on behalf of the Respondent:

- *R. Ford*
- *D. Lidgren*

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

The parties to this complaint advised the Board that this file, #70519, was the lead file, and that the issues, argument, and evidence in this case would be carried forward to other, similar assessment complaints.

Property Description:

There is an eight storey building on the subject property at 1300 8th Street SW. The building, "Barclay Square", was constructed in 1967, and contains 32,049 square feet ("sq. ft.") of office space. The Respondent has classified the building as a "B" class building. The subject property is bounded by 8th Street SW and 13th Avenue SW, and its land area is 16,215 sq. ft. The subject property is located in the "BL4" submarket area.

Issues:

The Board found the issues to be as follows:

1. Does the subject property suffer from chronic vacancy?
2. What is the correct rental rate for the subject property, $14 per sq. ft. or $15 per sq. ft.?
3. What is the typical vacancy rate for the subject property?
4. What is the appropriate cap rate for the subject property?
5. What is the correct assessed value for the subject property?

Complainant's Requested Value: $6,200,000

Summary of the Complainant's Submission

[1] The assessment amount is not reflective of the correct application of the assessment range of key factors and variables. These include location, parcel size, improvement size, land use,

and influences. The assessment amount is also not reflective of the correct application of either the comparison or income approach, and the Respondent has failed to recognize the negative influences that affect the subject property.

[2] The valuation model does not indicate the correct relationship between the subject property's characteristics as at December 31 of the assessment year, and their value in the real estate market. The assessment is neither fair nor equitable in relation to similar properties. Current performance of Barclay Square suggests this property is similar to "C" class office buildings, and "C" class buildings are assessed at $14 per sq. ft.

[3] Sales do not support the Respondent's overall rate per square foot for office space. The classification of the subject property is unfair, inequitable, and incorrect, and the assessment does not properly account for atypical deficiencies in the subject property as of the condition date.

[4] The rental rate applied to the subject property should be no more than $13 per sq. ft., and the vacancy rate should be no lower than 15%. The capitalization rate should be no lower than 6%. The non-recoverable amount should not be lower than 3%. The value attributed to the parking component is unfair, inequitable and incorrect (C-1, 6th page).

[5] The subject property has suffered chronic vacancy from 2008 to the present. Over that period the median vacancy comes out at 20.91%. While it is impossible to point to an issue that made it difficult to lease up this space, there are some potential issues. The first of these is the lack of amenities in the building. This is unusual because most buildings in the Beltline have some form of retail on the main level. The second possible issue is that the building owner has capped their costs, limiting how much they can charge their tenants, hence there is less money available for cosmetic upgrades (C-1, page 7).

[6] Further to this, there has been elevated vacancy for more than 36 months, and previous decisions of the Board suggest that this would be sufficient to qualify as chronic vacancy. The Complainant requests that the vacancy allowance for the subject property be increased to 20% in recognition of the problem.

[8] With respect to rental rates, the Complainant has determined that the Respondent has used only the last three months of the valuation period to derive the office leasing activity for the entire year. When other time frames are considered, the results of this rental rate study vary greatly, and are inconsistent with the time frames analyzed for other sectors. The Complainant has included the complete list of the Respondent's entire rental rates along with the median rates calculated for each time frame, and determined that the median leasing activity is dependent on the time frame considered.

[9] The only periods when the median is $15 per sq. ft. or more are the two month median, the four month median, and the five month median. All the other time frames indicate that the median rental rate should be between $14 to $14.50 per sq. ft. The Respondent used only the last three months of the valuation period to derive the office rental activity for the entire year. The Complainant has broken the lease analysis into its respective submarkets and determined the leasing activity in each market (C-1, pages 30 - 34).

[10] The Respondent's "B" class Beltline office rental rate study (2012 only) yields a mean of $15.03 sq. ft. and a weighted mean of $14.91 per sq. ft. (R-1, page 47). The Complainant's

analysis of the aforementioned study using a valuation range from July 1, 2011 to July 1, 2012 yields a mean of $14.74, and a weighted mean of $14.45 (C-1, pages 24 – 28). The Complainant's analysis of "B" class Beltline leases (with 620 12th Avenue SW left out) indicates a full year median lease rate of $14 per sq. ft. (C-1, page 30 – 34).

[11] When the Respondent was calculating the vacancy rate for Beltline properties, "AA", "A", "B", and "C" buildings were lumped together. The vacancy rate was not calculated this way for downtown or suburban properties. The Complainant has broken out each of the "AA", "A", "B", and "C" class buildings, and has calculated the vacancy for each classification. The average for "B" class is 11.25% (C-1, page 46 – 47).

[12] Now to capitalization ("cap") rates. The Respondent's cap study (C-1, page 49) includes the "Cooper Blok" building at 809 10th Avenue SW. This building should not have been included in the study because it was part of a portfolio sale of four buildings, which sold at a total cost of $142 million. Similarly, the "Keg building" at 605 11th Avenue SW (R-1, page 56) was not brokered, hence not exposed to the market. Therefore, it too should not have been included.

[13] The Respondent is currently using income parameters from July 1, 2010 to July 1, 2011 to calculate the cap rate for sales that occurred between July 1, 2011 and December 31, 2011. Thus the rents used for calculating the net operating income ("NOI") are offset six months from the sales that are being used to calculate the cap rate.

[14] The correct method is to use the income parameters derived from the period of time when the sales occurred. The Complainant suggests that the income parameters from July 1, 2011 to July 1, 2012 should be used to calculate the cap rate for sales that occurred from July 1, 2011 until July 1, 2012. The Respondent will protest, and argue that sales which occurred from July 1, 2011 to December 31, 2011 have more in common with the rents derived from July 1, 2010 until July 1, 2011 than the rents that have been derived from July 1, 2011 to July 1, 2012 (C-1, page 51).

[15] The Complainant counters the Respondent's argument by noting that because the Respondent uses the median rent from July 1, 2010 to July 1, 2011, there is no guarantee that the median rent calculated will approximate the leasing activity that occurred between July 1, 2011 to December 31, 2011 (C-1, page 51).

[16] By changing the rental rate parameter to $14 per sq. ft. for buildings in the BL4 zone, and to $15 per sq. ft. in the BL3 zone, and the vacancy rate to 11% for all "B" class buildings in the Beltline, the cap rate becomes 6%. Using these parameters results in an average and a median ASR of .9569 and 1.0072, respectively, with a coefficient of dispersion of 4.28 (C-1, page 53).

[17] When the *Duff* building at 525 – 11th Avenue SW and the *Grondin* building at 1451 – 14th Street SW are added into the analysis, the cap rate changes to 6.25%. The average and median ASR become 1.0296 and 09669 respectively, with a coefficient of dispersion of .0697 (C-1, page 57-58).

[18] The Respondent made the mistake of using incorrect vacancy and rental rates. These were derived for the subject property because the Respondent was looking at the Beltline as one homogeneous area. The Complainant provided evidence that the Respondent's method is incorrect. The reason the Beltline was separated into different sub-markets is to account for

differences between each sub-market in terms of rent and vacancy.

[19] In deriving the cap rate, the Respondent also made mistakes. Sales that should have been excluded were used. The sale of 809 10th Avenue was a portfolio sale. Due to the nature of portfolio sales it is not possible to determine the value attributed to each building that comprised the sale. Then there is 605 11th Avenue SW, which was not brokered, therefore not exposed to the market, a requirement of the definition of market value in section 1(n) of the *Act*.

[20] The Respondent used incorrect income parameters in deriving the cap rate, and failed to use all available valid sales. When the portfolio sale at 809 10th Avenue SW is excluded, the income parameters change. However, when the sales of 525 11th Avenue SW and 1451 14th Street SW are included in the analysis, the result is a derived cap rate of 6.25% (C-1, page 57)

[21] The Complainant has two options for valuation of the subject property. The first option is based on a rent rate of $15 per sq. ft., an office vacancy of 20%, and a cap rate of 6.25%. The result is a valuation of $6,510,000. With recognition of the exemption, the value is $6,257,103. The second valuation option, based on a typical vacancy of rate 11%, a rent rate of 14 per sq. ft., and a cap rate of 6.25%, results in a valuation of $7,370,000 (C-1, page 62).

Summary of the Respondent's Submission:

[22] The Complainant is requesting an office rental rate of $14 per sq. ft. based on leasing by submarket in the Beltline. The Respondent's 2013 "B" class Beltline office rental summary with a breakdown of leases in BL4 with commencement dates from July 1, 2011 to July 1, 2012 show that the resulting weighted average, $14.92 per sq. ft., amply supports the assessed rental rate of $15 per sq. ft. (R-1, page 21). Municipal Government Order 045-09 directs the use of weighted averages to determine typical rates.

[23] The Complainant has combined all Beltline office classes, and performed an analysis to determine that the overall typical office vacancy rate is 11%. The Respondent has reviewed the Complainant's "B" class office study, and made some needed changes. The corresponding study with corrections is provided (R-1, pages 22 – 23), and it indicates an office vacancy of 7.44%. With the corrections, even the Complainant's vacancy analysis comes in with a typical vacancy rate of less than 8%. The Respondent's own vacancy study is found at pages 49 to 53 of R-1.

[24] The Complainant requests a cap rate of 6.25%. The Complainant's assessment to sales ratio ("ASR") studies for the cap sales have been done incorrectly. The Respondent will speak to the sales the Complainant included in its cap rate study, two of which were excluded by the Respondent. One of these sales was that of the Duff building at 525 11th Avenue SW. The Duff building was purchased in 2011 for its potential of redevelopment, and sold 2013 for more than twice the original purchase price.

[25] Another sale relied on by the Complainant is the sale of the Grondin Building at 1451 14th Street SW. The Grondin building should be considered a retail building, not an office building.

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

[26] The Complainant asserts that there is chronic vacancy in the subject property. The Complainant claims this is due to lack of amenities in the subject property, such as retail businesses on the main floor. However, the Complainant also states that the owner of the building has *". . . put caps on their costs which limit how much they can charge their tenants. This restriction on how much the building owner can charge their tenants results in less money for cosmetic upgrades"* (C-1, page 7). This statement places the blame for greater than average vacancy squarely on the owner, not the building. In the view of the Board, to ground a claim for chronic vacancy the problem must lie with the building, and the problem must be one that is not easily remedied. There is no evidence in this case with respect to difficulty of remediation.

[27] The Complainant emphasizes the fact that the Respondent has rolled the nine submarket areas in the Beltline into one area, making the Beltline a single homogeneous market. The Complainant spent a great deal of time and effort to demonstrate to the Board that it was this newly created homogeneity that caused the assessor's typical rental rate for the subject property to be at $15 per sq. ft. instead of $14 per sq. ft.

[28] The Respondent, however, resurrected the BL4 submarket, and developed a B Class rental rate summary with leases that commenced from July 1st, 2011 to July 1st, 2012. The result is a weighted average of $14.92 per sq. ft. (R-1, page 21). That settled the issue of the correct rental rate as far as the Board is concerned. The typical rental rate is $15 per square foot.

[29] In regard to typical office vacancy, the Respondent responded to the Complainant's concerns about some of the properties included in the Respondent's B class vacancy study by making corrections and updating its vacancy study. One of the properties, 301 11th Avenue SW, was deleted, and rightly so, for there was nothing to show it was 100% vacant by the valuation date. In the result, the office vacancy came out at 7.44%, supporting the Respondent's typical vacancy rate of 8%. The Board finds the Respondent's revised vacancy study persuasive.

[30] When it comes to capitalization rates, the Complainant claims that the Respondent used income parameters from the period July 1, 2010 to July 1, 2011, to calculate the cap rate for sales that occurred between July 1, 2011 and December 31, 2011 (C-1, page 51). Thus the net operating incomes are alleged to be offset six months from the dates of the sales used to calculate the cap rate. The Complainant argues that the correct method is to use the income parameters derived from the period of time when the sales occurred, and suggests that the income parameters from July 1st, 2011 to July 1st, 2012 should be used to calculate the cap rate for sales that occurred from July 1st, 2011 to July 1st, 2012. With this argument the Board agrees, for otherwise the resulting cap rate would be an anachronism.

[31] The Respondent's capitalization ("cap") rate study includes the sales of five properties. In regard to the first two properties, the Keg building at 605 11th Avenue SW and the Cooper Blok building at 809 10th Avenue SW, the Complainant asserts that the Keg building had not been exposed to the market, and that the Cooper Blok building was part of a portfolio sale, therefore neither sale was should be relied upon for market value.

[32] In a similar vein, the Respondent advises the Board that the Duff building at 525 11th Avenue SW (from the Complainant's cap rate study) had been purchased for redevelopment, and later sold for more than twice the original purchase price. As for the Grondin building at

1451 14th Street SW, the Respondent states that it should be considered a retail building, not an office building. Yet another of the Complainant's sales, that of 1410 1st Street SW in the cap rate study at page 239 of the Complainant's rebuttal (C-1), is challenged by the Respondent on grounds that the sale was new evidence introduced in the rebuttal rather than in the Complainant's disclosure documents.

[33] In the result, the Board was left with three undisputed sales used in both the Complainant's and the Respondent's cap rate studies, i.e., 1520 4th Street SW, 906 12th Avenue SW, and 1207 11th Avenue SW. In deriving the cap rate from the three sales, the Board turned to the Complainant's cap rate study at page 239 of C-4. The Board was not able to rely on the Respondent's cap rate study because the origins of the NOIs used in the study could not be determined. The Complainant's study uses the typical rental rate of $15 per sq. ft., and the NOI's are the same as those in the 2013 assessments (C-4, pages 248, 253, 258). The Board determined the cap rate to be 6.15%, resulting in a capitalized value of $8,575,691.

The Board's Decision:

[34] The assessed value is $8,300,000 as rounded, taxable. It is so ordered.

DATED AT THE CITY OF CALGARY THIS 22nd **DAY OF** November **2013.**

[redacted]

Presiding Officer

Dissenting Decision:

[35] In previous years the Respondent had accepted "Chronic vacancy" when premises are shown to be vacant for more than three years. The subject "Barclay Square" office building is in sub market BL4 of Beltline containing 32,049 square feet as class B space, AYOC 1967 with typical 8% vacancy. The Complainant (MNP) in brief C1 pg 7 identifies the Barclay building as not typical of other Beltline buildings, in that this building has no amenity, recreational, or retail space which other comparable offices enjoy. The building owner is restricted by tenant charges, resulting in less money available for cosmetic upgrades.

[36] MNP offers numerous decisions (C1 Pg7) of chronic greater than 36 month vacancies. The Complainant asks for fairness and equity to calculate the subject at between 11%-20% vacancy as this building has "never had 8% vacancy."

[37] In evidence MNP produced a vacancy chart (C1 pg7) for the subject as follows:

Year	2008 vacancy 12.64%
Year	2009 vacancy 17.03%
Year	2010 vacancy 20.89%
Year	2011 vacancy 20.92%
Year	2012 vacancy 23.30%
January	2013 vacancy 32.65%

Median average @ 20.89%
(Excluding January)

[38] Further industry standard CRESA partners (C1 pg8-12) follows greater than typical vacancy for the subject ranging from lowest 2009 year @ 13.79% to a high of 30.06% in 2011 year capturing reports from 2008 to 2012

[39] Importantly the complainants brief includes rent rolls for vacancy as follows:

April 2008 @ 12.64%, July 1st 2009 @ 17.03%, July 1st 2010 @ 20.89%, July 1st 2011 @ 20.92%, July 2012 @ 23.37% and January 2013 @ 32.65% from C1 pages 13 to 18.

[40] In brief C1 pages 46/47 MNP have produced a homogenous Beltline "B" class office study correcting vacancies from Respondents AES sheets, resulting in 78 corrected vacancies @ 11.25%.

[41] Support for the Respondents all inclusive Beltline vacancy is 8.17% R1 pages 49-53. The Complainant notes this study includes some residential condominiums and retail from all sub markets with office buildings ranging from "A to C". The Respondent counters MNP's broader B class study to an actual 7.44% when correcting for non-typical, retail, restaurant and vacant space from ARFI's (R1 pg23). The Respondent refers to CARB decision 1424/2010P. This case refers to a purpose built building "and given that the improvements do not lend themselves to a multi-tenanted site, major renovations would be required if the building were leased to a single tenant" - - - "finding such a tenant would be challenging." In this appeal the subject was assessed with a 6% vacancy while MNP asked for 15% vacancy.

[42] In that conclusion "The Board finds the market value of the subject would be diminished from what would typically prevail" - - - "The Board concludes that a 10% vacancy allowance is justified. "The fullness of time might dictate that this allowance become more generous should elevated vacancy persist, or alternatively revert to typical." This in itself follows to support admission of greater vacancy allowance for the subject as non-typical.

[43] On the balance of evidence presented, the Complainant was able to convince this board member that the subject Barclay building does suffer unique circumstances relating to amenity space and building condition. It is highly unlikely that the owner could bear expenses to refit the subject to accommodate amenities given current leasing and markets of same. Rental rates for the subject are already comparable to BL4 market values. This therefore concludes this is a fault of the building rather than a management fault.

[44] This building would pale competing in open market sales comparing to similar. Clearly for reasons of evidence presented the assessment should reduce to $6,529,727 for a 20% vacancy allowance, 15 sq ft. rental and supporting a 6.15% capitalization.

[45] The truncated 2013 assessment is $6,290,000 on the taxable portion.

[46] Respectfully I concur with my colleagues on all other relevant issues herein.

DATED AT THE CITY OF CALGARY THIS 22nd DAY OF November 2013.

J. Kerrison

J. Kerrison
Board Member

<u>Exhibits</u>

C-1, Complainant's Submissions & Evidence

C-2, Complainant's Evidence

C-3, Complainant's Evidence

C-4, Complainant's Rebuttal

R-1, Respondent's Assessment Brief

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Appeal Type	Property Type	Property Sub-Type	Issue	Sub-Issue
CARB	Office	High Rise	Income Approach	Cap rate

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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.*