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:

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

and

The City Of Calgary, RESPONDENT

before:

H. Kim, PRESIDING OFFICER
P. Charuk, BOARD MEMBER
J. Pratt, BOARD 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 2013 Assessment Roll as follows:

ROLL NUMBER: **068110105**

LOCATION ADDRESS: **409 8 Ave SW**

FILE NUMBER: **70548**

ASSESSMENT: **$8,460,000**

This complaint was heard on the 30th of July, 2013 at the office of the Assessment Review Board located at Floor Number 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 5.

Appeared on behalf of the Complainant:

- *W. Van Bruggen*

Appeared on behalf of the Respondent:

- *K. Gardiner*

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

[1] The subject property was one of four C class office buildings in downtown Calgary under complaint by the Complainant's representative with broadly similar issues and argument to be considered. The Complainant requested that one property be considered in detail but that their presentations be carried forward to the other complaints with small modifications to the submissions based on site specific details. The Respondent agreed that it would be expedient to present their position on the four files in that manner.

[2] As the parties were in agreement, the Board agreed to proceed on that basis.

Property Description:

[3] The subject is a 4 storey, 48,267 sf office building on a 10,477 sf parcel located in the DT8 Sub Market area of downtown Calgary, known as the Montreal Trust Building. It is assessed on the income approach to value using the City's 2013 parameters for C class office buildings in DT8: 35,112 sf office space at a market net rental rate of $13/sf and 13,155 sf storage at $8/sf for a potential net income of $561,696. Vacancy of 6.75% for office and 10% for storage space is deducted. Vacant space shortfall based on operating costs of $16/sf office and $5/sf storage, and 2% non recoverables are applied and the resulting net operating income is capitalized at 5.5% to arrive at the original assessment under complaint.

Issue:

[4] The Complaint form identified a number of reasons for complaint. The only issue argued at the hearing was whether the capitalization rate should be increased to 7.0% from 5.5%.

Complainant's Requested Value: **$6,640,000**

Board's Decision:

[5] The assessment is confirmed at $8,460,000. The capitalization rate should remain at 5.5% and not be increased to 7.0% for the reasons detailed in CARB70510P-2013.

Complainant's Position:

[6] The cap rate for class C buildings in 2012 was 8% and for 2013 is 5.5%. The 2013 cap rate for class AA and A office buildings is 6.0%, as evidenced by the Assessment Explanation Supplement (AES) reports for the Bow, the Transcanada Tower, and Centrium Place, all premier buildings in the prime areas of the downtown core. The Complainant argued that it is unreasonable to consider class C buildings to have less risk to their income stream than class A. Historically there has always been a hierarchy of cap rates wherein class AA had the lowest cap rate and it increased for successive classes of building. The 2012 assessment was $10,370,000 and it more than doubled for 2013.

[7] The Respondent's cap rate study is flawed, as they analyzed sales in all of 2011 using 2012 typical income parameters, and sales in all of 2012 using 2013 income parameters. The

Complainant contends that this is incorrect, since 2012 income parameters are arrived at using information from July 1, 2010 to July 1, 2011. A sale in the latter half of 2011 should be analyzed using the 2013 income parameters that are derived from information from July 1, 2011 to July 1, 2012, the same time frame as the sale. Two class C sales were used to determine the 5.5% cap rate. The Complainant contends that neither are valid sales, and even if they were, the derived cap rate is incorrect:

- The Northland Building at 910 7 Ave SW sold on August 23, 2011 for a reported $38,606,000 however it was part of a portfolio sale of 29 office properties in Toronto, Ottawa, Edmonton and Calgary for a total purchase price of $831.8 million. The Complainant notes that the Respondent did not use portfolio sales in the cap rate study for suburban office buildings but relied on them heavily for downtown office buildings. The sale occurred in August 2011 but the Respondent's analysis uses the 2012 income parameters to arrive at a cap rate of 4.22%. The sale occurred after July 1, 2011 therefore it should be analyzed using 2013 parameters, resulting in a cap rate of 5.67%. The Complainant notes that the cap rate reported for the sale on RealNet was 7%.
- The Centennial Building at 816 7 Ave SW sold on January 18, 2012 for $6,020,000 but the Non Residential Property Sale Questionnaire indicates that the property was unlisted, and that it was not an arms length transaction. The purchase was motivated as the purchaser owned the adjacent building and intended to redevelop. The Centennial building's rent roll at time of sale showed annual rent of $762,424 compared to $399,875 market rent in the Respondent's analysis, and the Commercial Edge report on the sale indicates Reported NOI (Net Operating Income) of $421,400 and a Cap Rate of 7%.

[8] The Complainant presented two sales that were not considered by the Respondent:

- The Burns Building at 237 8 Ave SE transferred on August 17, 2012 just slightly after the valuation date for $13,100,000. The 2013 AES shows a $10/sf rate for Office Space Poor Location that is not supported in the sales literature. Applying the typical $13/sf office rate and 2013 income parameters, the cap rate is 6.27%. The Respondent typically applied a cap rate 0.25% lower than other C class buildings to 8th Avenue properties (DT8) so this sale supports the requested 7.0% cap rate.
- The KIK FM building at 1105 7 Ave SW sold on November 7, 2011 for $2,000,000. This corresponds to a cap rate of 10.55% using 2013 income parameters. That property was initially assessed at $5,800,000 for 2013 using the income approach but was amended to $2,000,000 on February 14, 2013 based on assessment for land value only. The Complainant contends that this is contrary to the Respondent's practice, whereby the land value is applied only when it is higher than the value using the income approach. The Complainant presented an excerpt from the Respondent's submission on a previous hearing to support this. The highest and best use would not be vacant land if the income parameters yield a greater value. This sale demonstrates that the 5.5% cap rate applied is too low.

[9] Third party reports do not report cap rates for C class buildings. The Complainant presented third party reports indicating the range of cap rates for A and B class buildings in the second quarter of 2012:

	CBRE	Colliers
AA	5.25 - 5.75%	
A	5.75 - 6.25%	5.5 - 6.0%
B	6.75 - 7.25%	6.25 - 7.0%

The ranges of cap rates shown supports the Complainant's position that class C rates should be no greater than 7.0% and that the Respondent's 2013 rates do not follow the hierarchy of cap rates normally found in the marketplace.

Respondent's Position:

[10] The Respondent agreed that historically, cap rates for class C were higher than for class A; however, the sales support the cap rates applied. The Respondent stated that unlike previous years, there were a number of sales of class A to C buildings in the analysis period (July 2011 to July 2012). There were two sales of class C buildings, both in the DT2 zone:

Address	Building	Registration. Date	Sale price	Area (sf)	AYOC	Typical NOI	Cap rate
816 7 Ave SW	Centennial Building	01/18/2012	6,020,000	27,203	1965	337,833	5.61%
910 7 Ave SW	Northland Building	08/23/2011	38,606,000	145,251	1982	1,628,440	4.22%

[11] The median and mean of the C class sales since July 1, 2011 were both 4.92% while A class were 5.64% and 5.61%, and B class were 4.82% and 4.65% respectively. Considering only sales in 2012, the median and mean of the C class sales were 5.61% while A class were 5.63% and 5.46%, and B class were 5.02 and 5.07. On that basis, the cap rates were set at 6.0% for A, 5.0% for B, and 5.5% for C.

[12] The Respondent stated that the use of the 2012 income parameters is appropriate in analyzing a sale in 2011. The parameters closest to the date of sale should be used, which is the July 1, 2011 valuation date for sales in 2012. The Respondent presented one 2013 CARB decision and two MGB decisions highlighting that a cap rate applied to NOI based on typical factors (inputs) must be a cap rate that also has been derived using typical NOI factors, and that typical factors for the year of sale should be used to maintain consistency.

[13] The Respondent defended the use of the Northland Building sale, presenting two 2013 CARB decisions where the sworn transfer values in portfolio sales were accepted as an indicator of market value. The Affidavit of Transferee was submitted along with corporate search documents to support the transfer value and to show the parties were unrelated. The Respondent stated that the Centennial building was reported on RealNet as brokered by CBRE Limited, contrary to the Sale Questionnaire response that it was "unlisted", which initially had a name that was blacked out. The question regarding arms length sale was initially answered "yes" and crossed out to change to "no". The Respondent insisted that both were valid sales that support the 5.5% cap rate.

[14] The Respondent presented a comparison of the Complainant's requested income parameters to those used to arrive at the 2013 assessment of the two buildings. The requested parameters would result in an Assessment to Sale Ratio (ASR) of 0.55 for the Northland Building and 0.75 for the Centennial Building compared to the actual 2013 ASRs of 0.82 and 1.02 respectively.

[15] The sale of the KIK FM building was not considered as it was an extreme outlier. There are no other sales that have cap rates of over 10%. The Burns Building is post facto but in any event it is on leased land and would not be considered a typical sale.

[16] The Respondent stated that with respect to equity, while the A class buildings have a 6.0% cap rate, rental rates applied are much higher, therefore the assessment per square foot is equitable. The Bow is assessed at $591/sf while the subject is at $245/sf, well within the range of the per square foot selling price of $221/sf for the Centennial Building and $263/sf for the Northland Building. The requested assessment would bring the per square foot value of the subject down to $170/sf, outside the range of similar buildings and would create inequity. The Respondent presented a list of 35 class C buildings in DT1, DT2, DT3, DT8 and DT9 that are all

assessed using the same income parameters as the subject.

Findings and Reasons:

[17] The capitalization rate should be 5.5%. While the Board agrees that it is unusual to have a class C cap rate of 5.5% when 6.0% is applied to class A, the cap rates are only a means to an end, which is to determine a value that is a reasonable estimate of the market value of the property, as required under the legislation. The relationship between 2013 class A and class C cap rates may be atypical; however the other income parameters are such that the overall value applied to class A compared to class C maintains equity.

[18] The Northland Building was part of a portfolio sale involving properties across the country. The Board was of the opinion that differences in local market conditions, applicable legislation and tax regimes could motivate an allocation of value for a property in a portfolio sale that might not accurately reflect the value for which it would have transacted in a standalone sale, and therefore gave little weight to the affidavit value.

[19] The Board finds the transfer of the Centennial Building to be a valid sale. The characterization of the sale as non-arms length was due to statements on the sale questionnaire that the purchaser was the owner of the adjacent parcel and wanted to redevelop. The Board does not consider this relationship to be non-arms-length, and was of the opinion that intent to redevelop is not unusual in a real estate transaction. Therefore, the Board was of the opinion that the purchase price reflects market value.

[20] The $175/sf assessed value of the subject is within a reasonable range of the $221/sf selling price of the Centennial building. The $138/sf result of the requested parameters would be significantly out of line. While the Complainant's arguments for the 7.0% cap rate was logical, and supported by the reported cap rates, it was clear that the actual income generated was different from the typical income applied using the parameters in place at the time of sale. Under those circumstances, applying the actual "going-in" cap rate to the lower typical income parameters would result in a value below market value, and would be inequitable with other similar properties in the municipality.

DATED AT THE CITY OF CALGARY THIS 3rd **DAY OF** September **2013.**

for **H. Kim**
Presiding Officer

APPENDIX "A"

DOCUMENTS PRESENTED AT THE HEARING AND CONSIDERED BY THE BOARD:

NO.	ITEM
1. C1	Complainant's Disclosure
2. R1	Respondent Disclosure
3. C2	Complainant's Rebuttal
4. C3	Complainant's Supplemental Rebuttal
5. R2	Respondent's Rebuttal CARB 72016P-2013
6. R3	Respondent's Rebuttal DL019/10
7. R4	Respondent's Rebuttal MGB123/10
8. R5	Respondent's Rebuttal CARB 70282P-2013
9. R6	Respondent's Rebuttal CARB 72586P-2013

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.

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Property Type	Property Sub-Type	Issue	Sub-Issues
(3) Office	Low Rise	Income Approach	Capitalization Rate