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:

12-10 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: 067233411

LOCATION ADDRESS: 1240 10th Avenue SW

FILE NUMBER: 71060

ASSESSMENT: $5,160,000

This complaint was heard on the 12th of July, 2012 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:

- *W. Van Bruggen*

Appeared on behalf of the Respondent:

- *D. Zhao*

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

No procedural or jurisdictional matters were brought to the attention of the Board.

Property Description:

The subject property, 1240 10th Avenue SW, is situated in the BL4 submarket sector of Calgary's Beltline. The subject property has a land area of 27,598 square feet ("sq. ft."), and abuts the CPR rail line to the north. On the land there is a one-storey office building that was constructed in 1973. The area of the building is 11,434 sq. ft. The Respondent has classified the building as a "C" class building.

Issues:

The Board finds the issues to be as follows:

1. Does the assessment of the subject property recognize the characteristics and physical condition of the subject property as at December 31 of the year prior to the year in which a tax is imposed, as required by Section 289(2) of the *Act*?

2. Has the Respondent failed to recognize negative influences that affect the subject property?

3. Should the rental rate for the subject property be $12 per square foot ("sq. ft.") and the capitalization rate ("cap rate") 6.0% if the subject property is assessed using the income approach to value?

4. Should the cost of removing the building on the subject property be recognized due to the fact that the Respondent assessed the property at land value only.

5. Is the assessment of the subject property inequitable when compared to two other properties assessed using the income approach.

6. Should the subject property be assessed using the Complainant's land approach?

Complainant's Requested Value: $2,300,000

Summary of the Complainant's Submission

[1] The amount of the assessment is not reflective of the correct application of the assessment range of key factors and variables, such as location, parcel size, improvement size, land use, and influences. Further, the assessment does not comply with Section 289(2) of the Municipal Government Act ("the *Act*") in that it does not recognize the characteristics and physical condition of the subject property as of December 31st of the year prior to the year a tax is imposed, i.e., December 31st, 2012 (C-1, 4th page).

[2] As of December 31st, 2012 the subject property was occupied as an office building, and there were no applications for development or development permits in place. There was nothing to indicate that a change in use was forthcoming or being contemplated. The subject building was an office building as of December 31, therefore should be valued as an office building.

[3] The Respondent did not rely on the correct application of either the comparison or income approach to value. Adjustments in connection with property rights, land use, market change, economic characteristics and physical characteristics are not correctly reflected in the assessment amount (C-1, 6th page).

[4] In particular, the Respondent has failed to recognize negative influences associated with the subject property. The subject property is contaminated with various substances, a result of previous land uses such as a chemical warehouse, a petrochemical company, smelting, railway operations, dry cleaning facilities, and diesel and fertilizer storage (C-2, pages 223 – 224).

[5] Remediation efforts are ongoing. The Respondent generally adjusts for contamination by applying -25% to the assessed value, but not in the case of the subject property. Negative influences, in this case contamination, a restrictive covenant, and proximity to train tracks, should support a negative adjustment of no less than 40% (C-1, 6th page), including 15% for contamination (C-1, page 14). The Complainant's land study can be found at page 143 of C-1.

[6] The assessment amount is neither fair nor equitable relative to similar properties in the jurisdiction. Sales comparables on the Respondent's website are not a comprehensive list of properties that sold between July 1st, 2010 and July 1st, 2012. The Complainant was able to locate 60 parcels of land between 9th and 17th Avenue, accounting for more than 1,000,000 sq. ft. of land appropriate for development. With that amount of land available, it is unlikely the owner would give up a fully occupied building to redevelop the land (C-1, page 16).

[7] The rental rate should be no more than $12 per sq. ft. and the cap rate 6.0% if the subject property is assessed using the income approach to value, as it should be. The current assessment is based on the notion that the highest and best use of the subject property is as land for redevelopment, an error that has resulted in an assessment in excess of market value, and one is inequitable when compared to similar competing properties (C-1, 6th and 7th pages).

[8] There is no reasonable probability that redevelopment of the subject property would be financially feasible, physically possible, and legally permissible as of the relevant assessment dates. If the Respondent insists on relying on highest and best use as land only, ready and waiting for redevelopment, the value of the improvement should be removed, for the

improvement is a cost to redevelopment.

[9] The subject property is leased out, and it is likely the cash flow will continue for at least the next five years. Given the Respondent's "C" class income parameters and a time horizon of five years, the present value of the income stream would be $571,796 (C-1, page 15).

[10] The subject property is constructed of reinforced concrete, hence the *Marshall and Swift* demolition costs estimator indicates demolition costs will be in the range of $3.21 to $4.95 per sq. ft., with a local multiplier of between 22% to 35%. The Complainant used the low end of both ranges, and determined that the demolition cost would be $3.91 per sq. ft. Since the area of the improvement on the subject property is 11,434 sq. ft., the cost of demolition would be $45,000. Therefore, the total cost of removing the improvement would be $580,000 plus $45,000, for a total cost of $625,000. Subtracting this cost from the current assessment results in $4,530,000 (C-1, page 16).

[11] Then there is the negative influence adjustment (-15%) for the railroad track. The Respondent no longer applies the adjustment in the Beltline, but continues to do so in the downtown core. The result of this inequity is an assessment that is neither fair nor equitable. If the contamination is recognized and an influence factor applied to the current assessment, the assessed value would be $4,250,000 (C-1, 8th page). If the subject property's actual use is recognized as the highest and best use, the assessed value would be $2,300,000, as based on the income approach (C-1, 7th page). Alternatively, there is the land approach, which, if done correctly at a land rate of $200 per sq. ft., would, with recognition of the influence for abutting the CPR track, result in a value for assessment purposes of $4,690,000 (C-1, page 143).

[12] When it comes to equity, the key rule is consistency. As stated in Dutchad Bil Investments Ltd. et al v. Area 19, *"The courts have regularly interpreted 'consistency' as the portion of market value being assessed (Bramalea, Lount, supra). In other words, if an appellant can show that other similar properties are typically assessed below actual value, then the subject should receive this benefit too."*

[13] Two "C" class Beltline buildings, 1005 11th Avenue SW and 615 11th Avenue SE, both with an FAR of 1, have been valued using the income approach. The Complainant is asking only that the subject property be fairly assessed compared to other "C" class properties in the Beltline. The Complainant's valuation request is based on the income approach, using the Respondent's income parameters, i.e., rental rate ($14 per sq. ft.), typical vacancy (8.0%), operating cost ($12 per sq. ft.), non-recoverable allowance (1.00), and a cap rate of 5.75%. The result is a value of $2,340,000 (C-1, page 30).

Summary of the Respondent's Submission:

[14] The Complainant is suggesting the possibility of three different market valuations for the subject property. First, a land valuation; second, the recognition of a contamination problem, and third, an income approach. The Respondent will provide the land sales and other information relied on to arrive at the assessed $220 per sq. ft. used to arrive at market value for vacant parcels as well as improved properties where the use of typical income parameters does not reach land value, as in the present case (R-1, page 4).

[15] The Respondent is not legislated to apply one specific approach to value in arriving at market value. In response to the Complainant's concept that an income producing property must be valued using the income approach, there is the sale of 1515 8th Street SW, an improved property. That property sold for much more than its assessed value. Using the direct sales approach with the vacant land rate, the aggregate assessment is much more reflective of market value (R-1, page 7).

[16] Thus it is proven that purchasers have paid more for properties than their income generating potential at the time of sale. The market value of any improved property may not be captured by the income approach as applied for assessment purposes. It sometimes occurs that at the time of valuation, typical income parameters for an improved type sit at a level that is incapable of producing estimates that approach the basic land value of the property.

[17] Beltline income parameters at the time of valuation have had an effect whereby the improvements to the subject property were exposed to a market-driven influence that resulted in an incapability of producing a capitalized income value that exceeds the established land value in the area. This has resulted in a capitalized income value that is incapable of reflecting market value. In short, the subject improvement is not the value driver of the property, thus the income from if cannot be capitalized to represent market value (R-1, page 8).

[18] Board decision ARB 1191/2010-P at point 6 states (R-1, page 9):

> *"The assessor went on to say that the value derived through application of the Income Approach, as applied by the Complainant was less than the bare land value estimated for the subject property and that is precisely why the land value has been applied. The reasoning of the Assessor is clear to the CARB and it is based on well founded valuation theory. If the improvements to a given property are of such an age or design or other influence that results in that property being incapable of producing a capitalized income value that exceeds the established land value, then the land value represents the market value of the property."*

[19] In further support of this point, the logical notion is that any willing seller would be hesitant to sell their property for less than its land value. Neighbouring properties have been valued in the same manner as the subject property, provided their respective income values are superseded by the established land value. This creates and maintains equity.

[20] The land use of the subject property is CC-X with an FAR of 5.0. This indicates that the maximum building area is much greater than the actual building area.

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

[21] The Board finds that the assessment of the subject property does not recognize the characteristics and physical condition of the subject property as at December 31 of the year prior to the year in which a tax is imposed, as required by s. 289(2) of the *Act*. In view of this finding, the issue becomes: What is the effect of failing to recognize the characteristics and physical condition of the subject property as at December 31 of the year prior to the year in which a tax is imposed? If there is a provision in the *Act* that would render the assessment null and void, the Board has been unable to find it. Nevertheless, the effect might well be an assessment that does not reflect market value. If the assessment does not reflect market value, it must be corrected, nothing more.

[22] The Board finds that the Respondent is not basing the assessment on highest and best use as alleged by the Complainant, although one might easily get that impression by the Respondent's use of words, i.e., *"The land use of the subject property is CC-X with an FAR of 5.0"* (R-1, page 9). It is the Respondent's Land Use Bylaw that *designates* the subject property as CC-X with an FAR of 5.0. The actual use of the subject property is far from what the Bylaw designates it to be.

[23] What the Respondent has done is assess the land of the subject property by the sales approach. The Respondent says the sales approach produces an assessment that reflects market value, defined in s. 1(1)(n) of the *Act* as the value that a property might be expected to realize if sold on the open market by a willing seller to a willing buyer. The Respondent's reasoning is that the subject property's land value is such that it supersedes any value attributable to the office building. As stated by the Respondent, the office building is not the "value driver". The Board agrees with the Respondent that in the case at hand, relying on the income approach to value the subject property would likely result in a value considerably below market value of the subject property.

[24] The Complainant asserts that the methodology used by the Respondent to determine the highest and best use for the subject property does not consider all necessary components. In particular, the fact that the building on the subject property is fully leased. Redeveloping the subject property would require demolishing the building, hence giving up the income stream. The Board agrees that neither of these costs were considered by the Respondent. The Complainant says the loss of the income stream over a period of five years would amount to a cost of $580,000, and the demolition $45,000, for a total of $625,000.

[25] The presupposition underlying the Complainant's argument is that a hypothetical prospective purchaser would be one who is ready and able to redevelop the subject property, and willing to purchase only at a price that recognizes the cost of demolition of the building and the loss of the income stream from the building. The Board accepts that a fixed demolition cost might be taken into account in reaching the purchase price, but the loss of the income stream over five years is a different matter. During the period required to obtain permits for development and attend to other related matters, the purchaser would be unlikely to demolish the building, for it would deny the purchaser the benefit of the income stream. The time from purchase to redevelopment would, however, be indeterminate, hence estimating the value of the loss of the income stream would be difficult if not impossible, therefore not likely to be taken into account in the sale price at the time of purchase. The Board notes that the Complainant derived the demolition cost using *Marshall and Swift.* In the view of the Board, to be taken seriously, the Complainant should have sought an estimate of the cost of demolition from a local contractor.

[26] The Board finds that the Respondent failed to recognize a negative influence that affects the property. The negative influence the Respondent failed to recognize is environmental contamination. Although the Respondent claims a negative influence for proximity to the CPR tracks, the Board notes that the 2013 Assessment Explanation Supplement ("AES") for the subject property at page 16 of R-1 shows a 15% negative adjustment for "Abutting a Train Track". The influence adjustment shown on the AES was not challenged by the Complainant during the hearing.

[27] Further to the issue of environmental contamination, none of the property addresses in the 2006 Phase II Environmental Site Assessment (C-2, page 261) are that of the subject

property. Nevertheless, the Board was able to determine by close examination of the air photo and the assessment map on page 10 of C-1, that one of the addresses in the 2006 Phase II Report, 1230 10th Avenue SW, is in fact the subject property.

[28] According to the Executive Summary of the Phase II Environmental Site Assessment, the primary contaminant is tetrachloroethylene. Tetrachloroethylene has been detected at a concentration *"in excess of the applicable site criteria in groundwater samples collected from boreholes MW2 and MW3."* Other hydrocarbons, i.e., benzene, toluene, ethylbenzene, xylenes, and metals are present, but below applicable regulatory criteria.

[29] The Board is of the view that the contamination of the subject property is likely to blight the subject property, hence preventing redevelopment of the subject property or making redevelopment much more expensive. The Board finds that the contamination warrants a negative influence adjustment to the assessment of 15%. There is nothing in the report of Troy Environmental Consulting contained in the Respondent's submission, R-1, that would convince the Board otherwise.

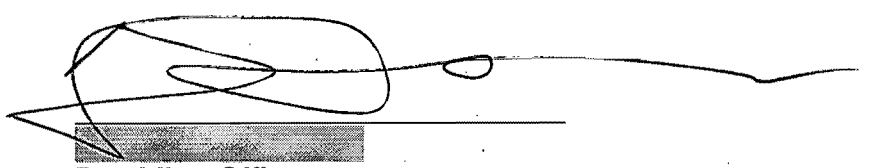
[30] The Complainant also submits that the subject property is assessed inequitably on grounds that two C class Beltline buildings, both with a floor area ratio ("FAR") less than one, have been assessed using the income approach. The Board notes that the Respondent seems to rely on the income approach only when there is a substantial building on a property. In other words, the income approach is relied on only when the resulting value of land and improvement exceeds the value of the land alone. Other than the fact that the two buildings are C class, Board finds insufficient evidence of their comparability to the subject property.

[31] As to the Complainant's sales approach, the land rate analysis at page 35 of C-1 is the same one that appeared in preceding files. Three of the six properties in the analysis are subject to "improvement adjustments", being amounts "stripped off" the properties. These improvement adjustments allegedly represent the depreciated values of existing properties, and deducting them is for the purpose of arriving at land values for each of the three properties. The problem the Board has with the improvement adjustments is that there has been no information, and there is no information now, with respect to the arithmetic method applied to achieve the depreciated values.

The Board's Decision:

[32] The Board adjusts the assessment for environmental concerns by negative 15% The assessment is reduced to 4,400,000, rounded.

DATED AT THE CITY OF CALGARY THIS 13th DAY OF November 2013.



Presiding Officer

Exhibits

C-1, Complainant's Evidence Submission

C-2, Complainant's Disclosure Package

C-3, Complainant's Second Disclosure Package

C-4, Complainant's Rebuttal

R-1, Respondent's Assessment Brief

For Administrative Purposes

Appeal Type	Property Type	Property Sub-Type	Issue	Sub-Issue
CARB	Office	Stand Alone	Income Approach	Cap rate

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.