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:

HCR LP (SC Calgary 2012) Inc. (Represented by Altus Group Limited), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

I. Weleschuk, PRESIDING OFFICER
H. Ang, BOARD MEMBER
T. Livermore, 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:	**068080902**
LOCATION ADDRESS:	**218 8 Avenue SW**
FILE NUMBER:	**72752**
ASSESSMENT:	**$2,780,000**

This complaint was heard on the 3rd day of July, 2013 at the office of the Assessment Review Board located at Floor Number 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 4.

Appeared on behalf of the Complainant:

- *M. Cameron*

Appeared on behalf of the Respondent:

- *E. Borisenko*

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

[1] Neither party objected to the members of the Board, as introduced, hearing the evidence and making a decision regarding this assessment complaint.

[2] The Board noted that the file included a completed copy of the Assessment Review Board Complaint form and Assessment Complaints Agent Authorization form.

[3] The Complainant Rebuttal was disclosed late (due June 24; received June 28) as a result of the Altus Group Limited (Altus) offices being closed for a number of days due to the flooding in downtown Calgary. The Respondent did not object to the Rebuttal being entered as evidence, given the circumstances. Board acknowledges Section 10(3) of Matters Related to Assessment Complaints Regulation, that with the consent of all parties, disclosure time can be abridged. The rebuttal evidence was heard.

[4] No further preliminary issues were raised by either party.

[5] To allow for a more efficient hearing, both parties agreed to carry forward evidence, questions and argument on issues relevant to the subject complaint from Hearing File No. 72598 (Decision 72598P/2013) which was heard by this Board earlier in the day.

Property Description:

[6] The subject property is a three level (lower, main and upper) retail building located at 218 8 Avenue SW, along Stephen Avenue in downtown Calgary (Sub-market area DT8). Stephen Avenue has been developed into a pedestrian friendly street, with a number of restaurants and bars. The subject is a multi-tenant property with 1,895 square feet (SF) of assessed storage area on the lower (below grade) level, 2,841 SF of retail space on the main level and 3,207 SF of office space on the upper level, for a total building area of 7,943 SF. The main level has direct access from the street, and operates as the Mango Shiva restaurant. The upper level has a separate access to the second level of the Scotia Centre. The current assessment is $2,780,000, using an Income Approach which assigns a different rental rate to the lower, main and upper levels.

Issues:

[7] The Complainant raised the first two specific issues identified below, and the Respondent raised the third issue.

Is the assessed rental rates for the main level correct?

Is the assessed vacancy rate correct?

Does the assessed value reflect the market value of the subject property?

Complainant's Requested Value: $1,980,000

Board's Decision:

[8] The Board confirms the 2013 assessment of $2,780,000.

Legislative Authority:

[9] Section 4(1) of Matters Relating to Assessment and Taxation Regulation (MRAT) states that the valuation standard for a parcel of land is "market value". Section 1(1)(n) defines "market value" as the amount that a property, as defined in Section 284(1)(r) of the Act might be expected to realize if it is sold on the open market by a willing seller to a willing buyer. Section 467(3) of the Act states that an assessment review board must not alter any assessment that is fair and equitable, taking into consideration (a) the valuation and other standards set out in the regulations. The issues raised in the Complaint may refer to various aspects of the assessment or calculation of the assessed value, and may be addressed by the Board. However, the ultimate test that the Board must apply is whether the assessed value reflects the market value of the assessed property.

Issue 1: Is the Assessed Rental Rates for the Main Level Correct?

Complainant's Position:

[10] The Complainant noted that the rental rates applied by the City for retail spaces in DT8 are different for each level and use. The Complainant took the position that the rental rate of $36.00/SF applied by the City to the main retail level for the 2013 assessment Income Approach calculation is not correct. The Complainant did not dispute the rental rate applied to the storage space in the lower level, or the office space on the upper level, so this is not at issue before this Board.

[11] The Complainant presented retail main level evidence (page 24, Exhibit C1) of two comparable leases with a lease rate of $31.00/SF and $21.00/SF, resulting in a mean and median of $26.00/SF. The Complainant argued that these two retail main lease comparables represented buildings that are similar to the subject, and noted that the subject only had access from Stephen Avenue (no direct access from the Scotia Centre mall). In rebuttal, the Complainant defended the position that these two leases were the best indication of the rental rate for the main floor retail for the subject.

[12] In rebuttal, the Complainant provided information on a number of the lease comparables presented by the Respondent (page 34, Exhibit R1), arguing that a number of the lease comparables were from buildings that were not comparable to the subject. The Complainant noted that the lease comparables within the Scotia Centre have access from both Stephen Avenue and the interior corridor of the Scotia Centre, which results in superior traffic through those retail outlets. The Complainant also noted that the leases in the Alberta Block (also known as Fashion Central) refer to spaces that have no direct access from Stephen Avenue, with access to the retail units via interior walkways. The Complainant concluded that only the lease comparables presented in Exhibit C1 are truly representative of the subject property.

Respondent's Position:

[13] The Respondent explained that the City has sufficient rental information to derive a specific rental rate for the lower, main and upper levels in DT8. This analysis is summarized on page 34 in Exhibit R1 for the retail main level. For the main level, based on nine leases with a mean of $45.44/SF and median of $45.00/SF, the City applied a rental rate of $36.00/SF. This analysis is also done ignoring three leases in the Alberta Block, which results in a mean of $35.67/SF and median of $35.50/SF, again supporting the $36.00/SF rate used by the City.

[14] The Respondent argued that the $21.00/SF lease rate for the main level in the Ward Block is below market, because there are some issues with the building. These issues include damage to the building as a result of construction of a building behind the Ward Block.

[15] The Respondent presented a summary of their vacancy rate and operating cost analysis (page 35, Exhibit R1) supporting the rates used in the 2013 Income Approach assessment calculation. Vacancy rate is indicated at 5% and operating costs at $12.00/SF. The operating costs were not at issue in this hearing.

[16] No evidence was presented regarding the rental rate applied for storage space or upper level office space, as this was not in dispute at this hearing.

Findings of the Board on this Issue:

[17] With regard to the rental rate for the retail main level, the Respondent presented nine lease comparables (page 34, Exhibit R1), including the two presented by the Complainant (page 24, Exhibit C1). The Board heard qualitative argument as to why some of the main level lease comparables should not be considered, because they were not comparable to the subject. Without some quantification to demonstrate the differences, the Board was not persuaded that these other lease comparables should be excluded from the analysis. That said, even excluding the Alberta Block leases, the remaining six leases including the two leases presented by the Complainant support the assessed rental rate of $36.00/SF for main level retail in DT8. The Board finds that the rental rate of $36.00/SF for main level retail space is appropriate. With regard to the lease comparable from the Ward Block, the Board heard somewhat conflicting evidence as to whether the lease rate was at market, and argument that there were some issues with the building that might result in the main level retail space being inferior to other main level retail located in DT8. For this reason, the Board put less weight on this comparable lease, when considering the main level retail lease comparables.

Issue 2: Is the Assessed Vacancy Rate Correct?

Complainant's Position:

[18] The Complainant presented a table showing the vacancy for all 34 properties that are located in Sub-market area DT8 (page 28, Exhibit C1), and considered by the City as being the Stephen Avenue properties. This table indicates that 69,361 SF of area is vacant, from a total available rentable area of 550,862 SF, resulting in a vacancy rate of 12.59%. This is the basis for the Complainant's request that the vacancy rate used in the 2013 assessment calculation should be 12.5%, not the 5% used by the City.

[19] This table includes the Bank of Montreal building (BMO) located at 140 8 Avenue SW, which has 100% vacancy (44,791 SF). The Complainant contended that this property was part of the supply for the Stephen Avenue rental market. To support this position, a copy of a marketing brochure used by the Taurus Property Group offering the retail portion of the building for lease (page 41-50, Exhibit C2) and a copy of a marketing brochure used by Colliers International (page 51-60, Exhibit C2) offering the upper office levels for lease were presented. An email from Chelsea Harding, Asset Manager for Steiner Properties Ltd. (building manager) dated June 19, 2013 is presented on page 62, Exhibit C2. This email states that the retail portion of the building was listed with Taurus on December 14, 2011 and the office portion was listed with Colliers in mid-January 2012. The email also states that the space will not be available before August 2013, at best. There is also "a binding deal in place for the office since September 2012 but the Tenant cannot take possession until the space is ready for occupancy."

[20] A copy of the 2012 Assessment Explanation Supplement and 2013 Non-Residential Properties-Income Approach Valuation (original) was presented on page 63 and page 64-65 respectively, in Exhibit C2. This was presented to demonstrate that the City was assessing the BMO building at the same rental rates as the other buildings in DT8.

[21] The Complainant concluded that the BMO building was actively being offered for lease since December 2011/January 2012, and that the City recognized it as being available for lease based on its 2013 Assessment valuation. Therefore, this building is part of the rental market on Stephen Avenue and should be included in the vacancy rate calculation.

Respondent's Position:

[22] The Respondent stated that the BMO building was not included in the City's vacancy study for DT8 properties because it has been vacant for a number of years and has been undergoing a total renovation, including replacing the roof, for more than a year. The Respondent pointed to the email from Chelsea Harding (page 62, Exhibit C2) which confirms that as of the condition date for the 2013 assessment year (December 31, 2012) the building was not in a condition that it could be leased.

[23] The Respondent stated that in response to its 2013 Assessment Notice, the City received a request from the building manager to inspect the building. Ms. Borisenko inspected the building on February 13, 2013 and concluded that the building was not capable of being occupied. She stated that the roof was still under construction at the time of her visit, and the interior was still essentially a shell. Photographs taken on this visit are presented on page 28-30, Exhibit R1. As a result of this visit, the City issued an amended Notice of Assessment based on land value and some improvement value. A copy of the amended 2013 Assessment Explanation Supplement is presented on page 31, Exhibit R1.

[24] The Respondent presented three pages apparently taken from the 2009 assessment complaint report (authored by Altus Group Limited) which indicated that the BMO building has been vacant since 2003 and that the cost to cure the physical problems exceed the value of the property (page 20-22, Exhibit R1). Assessment Review Board Decision 0503/2009-P was presented (pages 23-27, Exhibit R1). The Respondent noted that in that decision, the Board acknowledged the condition of the building and reduced the assessment to reflect the value of the property as vacant land.

[25] The Respondent argued that the property did not yet have an Occupancy Permit from the City. No evidence was presented to support this statement. There was no discussion of whether an Occupancy Permit is required before the property can be offered for lease, nor the role of an Occupancy Permit.

Findings of the Board on this Issue:

[26] Both parties use the same set of data, being the properties in DT8, to derive their vacancy rate. The only issue in dispute is whether the BMO building should or should not be included in the data set. The BMO building is one of the larger buildings in DT8, therefore how it is treated for the purpose of deriving a vacancy rate makes a big difference (12.59% if included and 4.85% if excluded).

[27] In considering the vacancy rate, the Board first needs to set out the test that it will apply to determine if the BMO building should be included in the database used to calculate the vacancy rate. As neither party provided any authority or detailed definition of vacancy rate, or more importantly how to calculate such a rate, the Board sought direction from information in the public domain. According to Appraisal of Real Estate (Eleventh Edition, Appraisal Institute, Chicago. Illinois. 1996):

> *"a vacancy rate is an allowance used in an Income Approach to reduce potential income attributed to vacancies or tenant turnover. .... The allowance is usually estimated as a percentage of potential gross income, which varies depending on the type and characteristics of the physical property, the quality of its tenants, current and projected supply and demand relationships, and general and local economic conditions. ... It reflects typical investor expectations over the specific holding period assumed or projected in the income capitalization approach." (page 489-490)*

The Board understands this to mean that in deriving a vacancy rate, it should be based on properties that are competing with one another in the same market for the same potential lessee. The definition of the market must be carefully considered, because all vacant space or property does not compete for the same potential lessee. The specific market may be defined by location, size of the space, utility of the space, price, amenities or some combination of these factors. Vacancy rate is defined not just by the existing space that is available, but also by the anticipated supply and demand considering new space coming into the market (if it will compete against the subject property type) and changes in economic climate that may affect supply and demand. In other words, what would a purchaser contemplating buying a revenue generating property in that "market" consider as the typical or expected vacancy rate for that property type?

[28] The Board notes that of the 34 DT8 properties presented on page 28, Exhibit C1, only six have any vacancy. The other 28 properties are all fully leased. Of the five with vacancies (not including the BMO building) the vacancy appears to be an entire floor, suggesting that it is in the process of renovations. There was some discussion to this effect, but no evidence was presented demonstrating that these properties were in fact undergoing renovations. The Board finds what appears to be a strong rental market for Stephen Avenue properties. Vacancy appears to be triggered by renovations, either initiated by the building owner to upgrade the quality of the space or by the lessee to add tenant improvements, and this vacancy tends to apply to only a portion of the building.

[29] The Board considered the BMO building to be atypical for the Stephen Avenue market, in that it has been vacant since 2003, and it is undergoing a total renovation (except for the exterior facade). Unlike the other buildings in the Stephen Avenue rental market, the BMO building is not temporarily under renovations or under renovations to allow for a transition of tenants. While the space in the BMO building is being actively marketed, the building was not close to a condition or state that tenants could take possession of the building as of the condition date (December 31, 2012), as the roof was still under construction. For these reasons, the Board finds that the BMO building is not part of the Stephen Avenue rental market as of December 31, 2012. Therefore, for the purpose of deriving the 2013 assessment and factors to be used in the Income Approach assessment calculation, the BMO building should not be considered in deriving the vacancy rate.

[30] While there was some suggestion that there was a lease in place for some of the space in the BMO building, no evidence was presented regarding when this lease comes into effect or for what portion of the building. Not having this detail also makes the use of the BMO building for vacancy rate purposes problematic.

[31] The Board finds that the vacancy rate used by the City in its Income Approach calculation for DT8 properties of 5% is supported by the vacancy rate evidence.

Issue 3: Does the Assessed Value Reflect the Market Value of the Subject Property?

Complainant's Position:

[32] The Complainant did not present any sales evidence. The Complainant presented evidence in rebuttal arguing that five of the six sales presented by the Respondent (page 45, Exhibit R1) did not meet the definition of market value.

[33] The Complainant presented an email from Janet Jesson, Real Estate & Development Coordinator for Joey Restaurant Group which purchased the Saltlik property (101 8 Avenue SW) on page 108, Exhibit C2. This email indicates that the vendor had a listing agent but that this was a sale negotiated between the two parties, likely because Joey Restaurant Group was the tenant and had a clause in the lease agreement that gave them a right of first refusal. No other evidence was presented regarding details of this transaction, or what the "right of first refusal" actually meant.

[34] The Complainant presented a press release from Allied Properties REIT and RealNet transaction summary (page 109-118, Exhibit C2) as evidence that the Bang & Olufsen property (129 8 Avenue SW) was part of a portfolio sale and argued that the price of $3,600,000 shown on the RealNet transaction summary sheet was not a reliable indication of market value.

[35] The Complainant presented a press release from Allied Properties REIT and RealNet transaction summaries (page 119-129, Exhibit C2) as evidence that the Alberta Block (805 1 Street SW) and Alberta Hotel (804 1 Street SW) properties were part of a portfolio sale and argued that the respective sale prices of $13,000,000 and $20,000,000 as shown on the RealNet transaction summary sheets were not a reliable indication of market value. The two remaining sales, the Thai Restaurant at $536/SF of building area and Leeson Lineham at $321/SF of building area average an indicated market value of $428/SF of building area. The Complainant argued that the Thai Restaurant is only 6,304 SF in size, therefore the per SF sale price likely overstates the market value of the subject property.

[36] The Complainant stated that the assessed value on a per square foot of assessed area for the subject is $476/SF, then argued that this was substantially more than the average sale value of $428/SF of building area and demonstrates that the subject is over assessed.

Respondent's Position:

[37] The Respondent presented six sales in the DT8 area on page 45, Exhibit R1 that indicate a mean of $444/SF of building area and a median of $457/SF of building area. The City has vetted all these sales and considers them market value transactions. This table of sales is also presented to demonstrate that the 2013 assessment reflects the sale prices, with a mean Assessment to Sales Ratio (ASR) of 0.98 and median ASR of 1.01. The Respondent argued that this demonstrates that the factors used by the City to prepare the 2013 assessments for the DT8 retail properties results in assessed values that reflect market value.

[38] The Respondent argued that the Complainant did not provide any evidence to show why the portfolio sales and the prices assigned to the properties within the portfolio sales were not the market value.

[39] The Respondent noted that the assessed value of the subject is $350/SF of building space, and falls within the range of sales presented on page 45, Exhibit R1.

Findings of the Board on this Issue:

[40] The Board is not convinced that the Saltlik sale or the three portfolio sale prices do not reflect their market value. In the Saltlik sale, it appears that both parties are sophisticated and know the market. There was no evidence presented to suggest that the vendor sold the property at a discount or that the purchaser paid a premium over market value. With regard to the portfolio sales, Real Estate Investment Trusts (REIT's) are a significant part of the market in downtown Calgary, therefore their involvement cannot be summarily dismissed simply because they are a REIT. REIT's are sophisticated property investors and would be expected to pay fair market value for properties they acquire. No evidence was presented to demonstrate that the sale prices assigned to these three sales does not reflect market.

[41] The Board understand that the purpose for presenting the table on page 45, Exhibit R1 is to demonstrate that the factors used by the City to calculate the 2013 assessments for retail buildings in DT8 results in assessed values that reflect market. The range of sales values is $321/SF to $536/SF of building area. This is a wide range, which is likely affected by the differences in building characteristics, including age of building, size and renovation history. The assessed value of the subject falls into the sales range.

[42] The Board finds that the 2013 assessment is within the range of sale prices and reflects the market value of the subject property.

Board's Reasons for Its Decision

[43] The Board noted that the Respondent provided a number of lease comparables to support the rental rates used by the City the main retail level. The Respondent's lease comparables included all the lease comparables presented by the Complainant. The Board concluded that the rental rate for retail main space in DT8 used by the City to prepare the 2013 assessment for retail buildings in DT8 is supported by lease evidence, and is appropriate.

[44] The Board considered the vacancy rate issue and specifically whether the BMO building should be included in the vacancy analysis. The Board concluded that the BMO building was not in fact competing in the Stephen Avenue rental market with the other 33 retail buildings in DT8, therefore it should not be included in the vacancy analysis. This confirmed the City's vacancy rate of 5% is reflective of the market.

[45] The Board notes that the assessed values for retail buildings in DT8 reflects the market value, based on an analysis of six sales. The subject assessed value falls into the range of value on a per square foot of building area basis, supporting the conclusion that the assessed value reflects its market value.

[46] While equity was not raised as a specific issue in this complaint, the Board finds for the reasons discussed above that the assessed value is fair and equitable, since all these properties were assessed using the same Income Approach calculation.

DATED AT THE CITY OF CALGARY THIS 25th DAY OF July 2013.

Ivan Weleschuk
Presiding Officer

APPENDIX "A"

DOCUMENTS PRESENTED AT THE HEARING AND CONSIDERED BY THE BOARD:

NO.	ITEM
1. R1	Respondent Disclosure
2. C1	Complainant Disclosure
3. R2	Respondent Rebuttal 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.

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Subject	Type	Issue	Detail	Issue
CARB	Retail	Stand Alone	Income Approach	Rental rates Vacancy rates Equity