



Calgary Assessment Review Board

DECISION WITH REASONS

In the matter of the complaint against the 2014 property assessment as provided by the *Municipal Government Act*, Chapter M-26, Section 460, Revised Statutes of Alberta 2000 (the Act).

between:

ARTIS Alpfordeau Ltd., COMPLAINANT
(as represented by Fairtax Realty Advocates Inc.)

and

The City Of Calgary, RESPONDENT

before:

I. Weleschuk, PRESIDING OFFICER
R. Deschaine, BOARD MEMBER
E. Reuther, 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 2014 Assessment Roll as follows:

ROLL NUMBER:	067027995
LOCATION ADDRESS:	833 4 Avenue SW
FILE NUMBER:	74729
ASSESSMENT:	\$69,340,000

This complaint was heard on 7th day of July, 2014 at the office of the Assessment Review Board located at Floor Number 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 8.

Appeared on behalf of the Complainant:

- *S. Storey, Agent – Fairtax Realty Advocates Inc.*
- *T. Omura, Appraiser – Omura Consulting Limited*

Appeared on behalf of the Respondent:

- *K. Gardiner, Assessor – City of Calgary*
- *H. Neumann, Assessor – City of Calgary*

Procedural or Jurisdictional Matters:

[1] The Board as constituted to hear and decide on this matter was acceptable to both parties.

Property Description:

[2] The subject property is located at 833 4 Avenue SW, in the Downtown 2 (DT2) Area. The property is a twelve storey office building with a total of 156,402 square feet (SF) of assessable building area, all assessed as office space. The property also has 89 underground parking stalls. The building was constructed in 1981 and has apparently been renovated periodically. The property is considered a B Quality Class Downtown Office building for assessment purposes.

[3] The 2014 property assessment is calculated using the Income Approach. The net operating income (NOI) of \$3,530,000 is divided by the capitalization rate of 5.00%, resulting in a value of \$70,600,160, less \$1,260,000 of exempt value, for an assessed value of \$69,340,000 (rounded). The specific factors used to prepare the assessment for this B Quality DT2 property are presented in the table below.

Sub-components	Area	Rental Rate (\$)	Vacancy Rate %	Operating Cost (\$/SF)	Non-recoverable %
Office	156,402 SF	22.00/SF	3.50	16,50	2.00
Parking	89 stalls	4,200/stall	0.00	0.00	2.00

Issues:

- [4] The Complainant stated that the 2014 Assessment is incorrect for the following reasons:
- The capitalization rate of 5.00% is not correct. The correct capitalization rate for B Quality Office properties in DT2 is 6.25%.
 - The office rental rate of \$22.00/SF is not correct. The correct office rental rate for this property is \$20.00/SF.

Complainant's Requested Value: **\$51,750,000**

Board's Decision:

- [5] The 2014 Property Assessment of \$69,340,000 is confirmed.

Legislative Authority, Requirements and Considerations:

[6] 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.

[7] The Board notes that the words "fair" and "equitable" are not defined in the Act or its Regulations. Equitable is defined in Black's Law Dictionary (Seventh Edition, West Group, St. Paul, Minnesota, 1999) as "just, conformable to principles of justice and right". For the purpose of this decision, the Board considers an assessment that reflects market value to be "fair and equitable" as the taxpayer is being assessed in accordance with the assessment standard applied to all properties in that property category.

Issue 1: What is the correct capitalization rate for B Quality DT2 property?**Complainant's Position:**

[8] The Complainant raised the issue of vertical inequity related to the capitalization rates assigned by the City to the various quality classes of downtown office buildings for the 2014 Assessment, and made the following points:

- This issue was identified during the previous year's assessment complaint process and has not been corrected by the City in the capitalization rates used in this assessment year.
- The capitalization rate assigned to Class AA, A and C downtown office buildings is 5.75%, while the capitalization rate assigned to the B Class downtown office buildings is 5.00%. The Complainant stated that this is illogical. In theory and in practice, better quality buildings (newer) should have lower capitalization rates than poorer quality buildings. Therefore, the capitalization rate for Class B buildings should be greater than Class AA and A, but less than Class C. The fact that this is not the case clearly shows that the City has made an error in how it calculates the capitalization rate.
- Downtown office buildings sell based on their cash flow; the price paid for a building is based on the contract rents in place, plus the potential purchaser's expectations related to lowering operating costs, etc. The sale price of these buildings, used to calculate the capitalization rate, is therefore the leased fee value of the property, not its fee simple value.
- The City uses the sale price without adjusting this leased fee value to a fee simple value, and therein lies the reason that the City has derived an erroneous capitalization rate for all classes of office buildings in the downtown core.

[9] The Complainant presented a Capitalization Study of Class "B" Downtown Highrise Offices prepared by Mr. Tony Omura, an accredited appraiser (page 22-38, Exhibit C1 with support material also presented in Exhibit C1). Mr. Omura, presented as a witness, summarized his findings and answered questions regarding the study. This is a similar study presented at some Board hearings in relation to B Class Downtown office buildings for the 2013 Assessment year. The following key points were made by Mr. Omura:

- The premise of the study was to determine the capitalization rate for Class B Downtown office buildings, accepting that, "*the capitalization rate must be higher than "A" class properties the Colliers survey indicated at 5.25% to 5.75%.*" (page 31, Exhibit C1).
- The study used six sales taken from the list of downtown office sales provided by the City (page 80-81, Exhibit C1) in response to an information request by the Complainant. A summary of the study and its results is presented on page 30, Exhibit C1.
- The net operating income (NOI) is based on the actual contract rents in place at the time of sale, and averages \$26.90/SF. This rate is supported by some Cresa Average Net Rental Rate information that indicates a rental rate of \$26/SF for all classes of downtown Calgary office buildings.

- The NOI is taken from sales detail sheets provided by the client and included in Exhibit C1. Where an NOI is not shown on the sales detail sheets, the information was provided by the purchaser. The source material to support the NOI's provided directly by the purchasers was not included in Exhibit C1.
- By using the actual leases in place at the time of sale for each of the Comparable Sales used in the study, a leased fee capitalization rate of 5.75% - 6.50% was derived. This range of rates is supported by the Second Quarter (Q2) Colliers International Capitalization Rate Report presented on page 29, Exhibit C1.

[10] Mr. Omura stated that by calculating the leased fee capitalization rate, the issue of vertical equity related to the capitalization rates for downtown offices in Calgary is resolved. The City's rate of 5.75% for Class AA and A fits with the calculated rate of 5.75% - 6.50%, say 6.25% as used by the Complainant in calculating its requested assessment.

[11] The Complainant offered a number of suggestions as to how the City might address this issue of vertical inequity related to the capitalization rate for downtown offices, so that this issue does not occur in subsequent years.

[12] In the closing statement, the Complainant stressed that the price for downtown office buildings is based on the revenue that the respective building generates. The sale price is not a fee simple value, but rather a leased fee value. If typical rates are applied to the leased fee sale price, the resulting calculation of the capitalization rate is incorrect. The Omura study, supported by third party industry data, confirms that the correct capitalization rate for B Class Downtown offices is 6.25%.

Respondent's Position:

[13] The Respondent presented its 2014 Capitalization Rate Study – Downtown B (page 51, Exhibit R1) with five of the six sales used common with those in the Omura Study. The Respondent's analysis applies typical rates to derive typical NOI, used to calculate the capitalization rate, which ranges from 4.35% - 5.51%. Based on this analysis, the City used a capitalization rate of 5.00% to calculate the 2014 Assessment for B Class Downtown Offices. This table also shows that the 2014 Assessment is very similar to the time adjusted sale prices for these six Comparable Sales. Exhibit R1 includes support data for the capitalization rate data.

[14] The analysis presented on page 54, Exhibit R1 also presents a column that shows that the sale price for these six Comparable Sales (sales occurring between June 2012 and February 2013) ranged from \$345/SF to \$507/SF. The Respondent noted that the requested assessment translates into a price per square foot of about \$330, which is substantially lower than the range of sales. These sale prices support the 2014 Assessment, which translates into a per square foot value of \$443, which is within the range of sale prices. Further, this analysis showed that the assessment to sales ratio resultant using the Respondent's method produces a mean value of 0.97, but a mean value of only 0.68 using the Complainant's method.

[15] In response to the issue of vertical inequity between the capitalization rates assigned to various classes of downtown office buildings, the Respondent stated that the capitalization rates were derived from an analysis of sales for each quality class. Furthermore, that the capitalization rates used to prepare the 2014 Assessments were good indicators of the market value of these properties, regardless of whether the rates conformed to theoretical expectations or patterns.

[16] The Respondent argued that the City is required to prepare assessments using mass appraisal, which requires the use of typical rates. The capitalization rate presented by the Complainant and derived using actual NOI is the actual capitalization rate, not the typical capitalization rate. The Respondent noted that the Omura study uses a rental rate that averages \$26.90/SF, while the City uses \$22/SF as its typical for B Class DT2 offices in its analysis. The Respondent also noted that it is not clear how the NOI applied to the Comparable Sales used in the Omura Study were derived, as they were apparently taken from third party sales detail sheets or were provided via personal communication, the latter not in evidence before this Board.

Findings of the Board on this Issue:

[17] Each party presented its capitalization rate analysis. The Complainant's capitalization rate is based on actual rates while the Respondent's rate is calculated using typical factors. Both approaches are acceptable methodologies, provided that they are applied correctly and consistently.

[18] The Board notes that in the calculation of the requested assessment on page 5, Exhibit C1, the Complainant uses all the typical rates used by the City to prepare its 2014 Assessment except for the rental rate for B Class DT2 offices (see discussion below) and the capitalization rate. The Complainant uses the capitalization rate of 6.25% derived using actual factors (NOI based on leases in place) and then applies this rate to an NOI derived using primarily the City's 2014 typical rates. The Board finds this calculation to be an inconsistent application of the rates, as has been addressed in various Board and court decisions (i.e. *Westcoast Transmission Company Limited v. Assessor of Area 9 – Vancouver BC 235, (1987) B.C.J. No. 1273*). As a result of this inconsistent methodology, the Board does not accept the capitalization rate of 6.25% requested by the Complainant as correct for the purpose of calculating the 2014 Assessment for B Class Downtown Offices. The Board prefers the capitalization rate presented by the Respondent of 5%, based on its analysis using typical factors and applied using typical factors.

[19] The Board notes that the Complainant did not specifically dispute any of the typical factors used by the City in its capitalization rate study, nor how the typical capitalization rate was derived. Rather, the Complainant argued that the sale prices represented the leased fee estate, and so resulted in an inconsistent use of typical rates applied to a lease fee sale price. In other words, the Complainant's argument was not with the detail but the concept.

[20] The ultimate issue before the Board is whether the assessed value reflects the market value of the subject property. The sales data provided by the Respondent demonstrates that the 2014 Assessment of about \$443/SF is within the range of sale prices of the six Comparable Sales presented (five of which are common to the Omura Study). The Board also notes that the subject property sold on June 15, 2012 for \$63,725,000 (page 160-162, Exhibit R1) and that the market has subsequently trended upward (page 63, Exhibit R1). This further supports the 2014 Assessment as correct.

[21] The Board notes the issue of vertical inequity raised by the Complainant, but this is not an issue that the Board has any jurisdiction over. The Board has authority to review the assessment complaint related to the property before the Board, and either confirm or change an assessment that does not reflect market value, or is not fair or equitable (Section 467 of the Act). How the City creates its assessment models and derives its input factors for those models is outside the scope of the Board. For this reason, the Board cannot address some of the broader issues and suggestions presented by the Complainant related to the City's assessment policies and procedures.

Issue 2: What is the correct office rental rate for the subject B Quality DT2 property?

Complainant's Position:

[22] The Complainant presented its Class B Current Market Lease analysis on page 8-10 of Exhibit C1. This analysis consists of leases signed since January 1 2012 in six office buildings that form part of the portfolio owned by the subject owner. The Complainant stated that they only have access to data from buildings owned by their client, but that this is a representative sample of B Quality office building leasing in the downtown. This analysis supports a rental rate of \$20.00/SF for B Quality DT2 office space.

[23] The Complainant referred to the vacancy rate for this type of office property, and while vacancy is not an issue before this Board, noted that it has to be considered as it influences rental rates.

[24] The Complainant referred to the subject rent roll (page 15-21, Exhibit C1) and noted that there was only one recent lease in the subject building, signed in April 2013 for \$23.00/SF. The Complainant stated that this renewal included three months free rent, therefore the effective rental rate was \$21.85/SF.

[25] In response to the 2014 B Class DT2, 3, 9 Office Rental Analysis presented by the Respondent (page 37-38, Exhibit R1), the Complainant argued that the rental rates did not capture any inducements or tenant improvements that are a typical part of the rental market and result in the effective rent rate being less than the contract rent. Therefore, this analysis overstated the effective rent being received by the owner of B Class office properties.

Respondent's Position:

[26] The Respondent presented a rebuttal to the Complainant's office rental rate analysis on page 23 of Exhibit R1. Except for the lease from the subject property, all the other properties used in the analysis are not B Class offices and/or are not located in DT2. Therefore, the analysis is not specific to Class B Office rental rates in DT2.

[27] The Respondent presented its 2014 B Class DT2, 3, 9 Office Rental Analysis on page 37 and 38 in Exhibit R1. This analysis consists of 43 leases commencing between July 1, 2012 to April 1, 2013 in B Class office buildings located in DT2, 3 and 9. This analysis indicates a mean of \$21.67/SF, a median of \$22.00/SF and a weighted mean of \$21.94/SF. This analysis supports the \$22.00/SF rental rate applied to B Class office space in DT2.

Findings of the Board on this Issue:

[28] Both parties presented a rental rate analysis.

[29] The Complainant's rental rate analysis included leases from various office building classes located across the downtown area, as well as one suburban office. The Board acknowledges the difficulty that a Complainant may have in obtaining rent roll information. Nevertheless, this analysis does not persuade the Board that the correct rental rate for B Class office space in DT2 should be \$20/SF. The Board notes that the most recent lease in the subject building (April 2013) is at \$23/SF. While there may have been some inducements or a rent free period associated with this lease, there was no evidence presented verifying this was the case or what the details of these inducements were other than the Complainant's statement to that effect.

[30] The Respondent presented its rental rate analysis that is specific to B Class offices located in DT2, 3, 9, which supports the \$22/SF rental rate used to prepare the 2014 Assessment. The Board prefers the evidence presented by the Respondent, as it is specific to the subject property type and represents a more comprehensive market analysis. The Board is not persuaded by the Complainant's argument regarding the weaknesses in this analysis.

[31] The Board finds that the rental rate for B Class office space in DT2 is \$22.00/SF, as used to prepare the 2014 Assessment.

Board's Reasons for Decision:

[32] The 2014 Property Assessment of \$69,340,000 is confirmed. The 6.25% capitalization rate is derived by the Complainant using actual NOI, and then applied to typical rates derived by the City to calculate the Complainant's requested assessment. This is an inappropriate and inconsistent application of the Income Approach methodology, therefore the Board prefers the Respondent's capitalization rate as used to prepare the 2014 Assessment. The Board finds that the rental rate for B Class DT2 office space is \$22/SF, as supported by the evidence presented.

DATED AT THE CITY OF CALGARY THIS 7 DAY OF August 2014.

A handwritten signature in black ink, appearing to read 'I. Weleschuk', written over a horizontal line.

I. Weleschuk
Presiding Officer

APPENDIX “A”

**DOCUMENTS PRESENTED AT THE HEARING
AND CONSIDERED BY THE BOARD:**

NO.	ITEM
1. C1	Complainant Disclosure
2. R1	Respondent 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	Sub-Type	Issue	Sub-Issue
CARB	Downtown Office	B Class DT2	Capitalization Rate	Rental Rate