



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:

FIRST REAL PROPERTIES LIMITED
(as represented by Avison Young), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

S. Kashuba, PRESIDING OFFICER
A. Wong, 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 2014 Assessment Roll as follows:

| | |
|--------------------------|--------------------------|
| ROLL NUMBER: | 068053404 |
| LOCATION ADDRESS: | 329 – 5 Avenue SW |
| FILE NUMBER: | 76877 |
| ASSESSMENT: | \$122,920,000 |

This complaint was heard on the 8th day of August, 2014 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:

- C. Hartley Agent, Avison Young Property Tax Services
- A. Farley Agent, Avison Young Property Tax Services

Appeared on behalf of the Respondent:

- H. Neumann Assessor

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

[1] No procedural or jurisdictional issues were raised. The Board continued to hear the merits of the complaint.

Property Description:

[2] The subject property, located at 329 – 5 Avenue SW and currently known as 333 Fifth Avenue, was constructed in 1978. The building has a net rentable area of 245,635 square feet over 19 floors, office space, retail space, storage space, and 124 parking stalls. The average floor plate in the property is 15,600 square feet. There is no retail on the main level which is rare for a Class A- property in the downtown core (DT1). The only retail space can be found on the +15 level pedway. The current assessment is \$122,920,000.

Issues:

[3] What is the correct classification for the subject property, Class A- or the requested Class B?

[4] What is the correct capitalization rate to be applied against the subject property, the City's 5.75% for the subject's classification of Class A- or a capitalization rate of 5.75% applied to the subject's Class B classification?

Complainant's Requested Value: \$102,480,000

Board's Decision:

[5] It is the decision of the Board to confirm the assessment of the subject property for 2014 at \$122,920,000.

Position of the Parties

Complainant's Position:

[6] Located in the downtown core (DT1), the City has assessed the subject as a Class A-office building. However, according to the Complainant, the property does not fit into the Class A category. Recent leasing activity, the lack of retail space, and the age of the building would suggest that the subject is incorrectly classified.

[7] As a result of the foregoing and since the subject property exhibits those characteristics which are found in Class B buildings, the subject should be re-classified as a Class B building.

[8] The City applies a single capitalization rate for a specific group of buildings. For Class A- buildings, the City applies a capitalization rate of 5.75%. However, it is inappropriate to arbitrarily use a single capitalization rate for a class of properties.

[9] The City applied the typical Class A- market rent of \$30.00 per square foot to the subject property without regard for the specific characteristics of the subject property (Exhibit C-1, pages 12 – 14).

[10] By re-classifying the subject from a Class A- building to a Class B building and applying a market rent of \$25.00 per square foot in the Pro Forma (Exhibit C-1, page 12), one arrives at a net operating income of \$6,303,054. This would then result in an assessment value of \$102,484,330.

[11] In doing this calculation, it is the position of the Complainant that a capitalization of 5.75% should be applied to this Class B building, as opposed to the City's use of a capitalization rate of 5.00% for all Class B buildings in the downtown core. However, even if one were to apply a capitalization rate of 5.00%, this would result in a reduction in the assessment amount.

[12] In addressing the question of the classification for the subject, the Complainant submitted that the exterior of the structure was of concrete slab, and hurriedly put together by the developer in order to capture positive market conditions (Exhibit C-1, page 20). The photographs submitted would support the view that the subject does not deserve a Class A-designation but rather a Class B designation (Exhibit C-1, pages 20 – 32).

[13] Recent leasing activity in the subject property (Exhibit C-1, page 34) would indicate that the range is from \$17.00 to \$34.00 per square foot with a mean of \$26.75 per square foot. These lease rates do not support the Respondent's application of a lease rate of \$30.00 per square foot.

[14] The Complainant's request for a reduction in the lease rate is further supported when one examines the lease rates of 23 Class A- properties (Exhibit C-1, page 38) in DT1 and 21 properties in DT1,8 (Exhibit C-1, page 39). However, it should be noted that the mean lease rate of \$31.72 is for DT1 and DT1,8 buildings which are classified as Class A- and cannot be applied to the subject property which exhibits the characteristics of a Class B building.

[15] Lease rates within 15 Class B buildings located in DT1 and 15 buildings located in DT1,8, which exhibit characteristics similar to those found in the subject property, indicate that a lease rate of \$25.00. In order to attain a measure of fairness and correctness, a value of \$25.00 per square foot should be applied to the subject property (Exhibit C-1, pages 42 – 43).

[16] Further support for a reduction in the lease rates applied to the subject property is provided by examining the assessments of similar properties (Exhibit C-1, page 54).

[17] By way of conclusion, the Complainant produced an example of a Pro Forma in which a rental rate of \$25.00 per square foot is applied. The City's Class B inputs are used along with a capitalization rate of 5.00% to arrive at a value of \$117,861,079 (Exhibit C-1, pages 65 - 66). This translates to an assessment of \$479.82 per square foot. In contrast, the assessments of similar properties range from \$446.56 to \$592.89 per square foot (Exhibit C-1, page 67), while the assessment of the subject property reflects an assessment of \$513.20 per square foot.

[18] In their request to re-classify the subject property from a Class A- building to a Class B building, the Complainant presented the typical Class A characteristics (Exhibit C-1, pages 88 - 104). Typical Class B characteristics are also presented by the Complainant (Exhibit C-1, pages 105 - 124).

[19] Seven Class A- buildings located in the downtown core, DT1, were presented for examination. The Complainant pointed out that these buildings did not have characteristics that mirrored those of the subject property (Exhibit C-1, page 90). On the other hand, the eight Class B buildings selected in the downtown core (DT1), did exhibit characteristics similar to those found in the subject (Exhibit C-1, page 106). From this, one can only conclude that the subject property is incorrectly identified as being a Class A- building rather than a Class B building. This is further supported by Class B building comparable leasing activity (Exhibit C-1, pages 125 - 127).

[20] The method by which the City calculates capitalization rates by looking at market rents for transactions occurring in the fall of a given year is faulty. The more appropriate methodology would be to use the forward looking market rent for sales that occurred in the fall of the previous year (Exhibit C-1, pages 180 - 194). This methodology would then reflect the proper use of the net operating income as well as the actual office rental rent based on current leasing within each subject property.

[21] In support of their request for a reduction in the assessment amount, the Complainant presented several precedent cases (Exhibit C-1, pages 132 - 177 and pages 215 - 229).

Respondent's Position:

[22] The Pro Forma (Exhibit R-1, pages 13 - 14) presents the Respondent's income approach to valuation in which a net market rental rate of \$30.00 per square foot is used.

[23] A list of 16 downtown properties (Exhibit R-1, page 20) is presented by the Respondent. Each is classified by the City as falling into the Class A- category. This classification is supported by Cresa and Altus InSite.

[24] The leases for the subject, as requested under the City's request for information, are presented in Exhibit R-1, pages 38 - 69. Of particular note (Exhibit R-1, page 71) is the fact that the subject property has several leases commencing in the 12 months leading up to the valuation date which fully support a lease rate of \$30.00 square foot. Further to this, it should be noted that all Weatherford leases have a July, 1999 commencement date. As a result of their age, these should all be removed from the analysis. By removing these, a lease rate of \$30.00 per square foot applied to the subject property is supported (Exhibit R-1, pages 72 - 73).

[25] As to the question of the application of a capitalization rate for Class A and Class B buildings, it is the opinion of the Respondent that these rates are only a means to determine a value that is a reasonable estimate of the market value of the property. Income parameters

might be such that the overall value applied to Class A buildings compared to Class B buildings does maintain equity (Exhibit R-1, pages 75 – 76).

[26] In developing its Pro Forma, the City's methodology in applying the typical net operating parameters closest to the sale date in an increasing or a decreasing market situation (Exhibit R-1, pages 77 – 79) provides the most reliable results.

[27] By way of conclusion and to request that the Board confirms the assessment of the subject property at \$122,920,000, the Respondent presented Board Order MGB 145/07 (Exhibit R-1, pages 109 – 147), MGB No. DL 019/10 (Exhibit R-1, pages 148 – 152), and several CARB decisions (Exhibit R-1, pages 153 – 189).

Complainant's Rebuttal Submission:

[28] The trends in capitalization rates utilized by the Respondent are incorrect. In support of this position, the Complainant provided two third-party reports, a Canadian Cap Rate Survey (Exhibit C-2, pages 3 – 5), and a Colliers International Canada Cap Rate Report (Exhibit C-2, pages 10 – 21).

[29] In reflecting upon capitalization rates for various classifications, it is the submission of the Complainant that the capitalization rates are higher as the quality of the building decreases. This, according to the Complainant, directly correlates with the varying degrees of risk with each class of assets. Class A properties have less risk associated with them than do Class B properties and therefore have lower capitalization rates.

[30] The purpose of the two third-party reports was to establish that the most important leasing information for determining market rent at the time of the sale of a property would be the most recent leasing up to the sale date and any known future leasing contracts in place.

[31] The City uses post facto leases which occurred after the valuation date of July 1, 2013 to support the assessed rate (Exhibit C-2, pages 22 – 23). This results in the use of erroneous lease rates leading to an incorrect NOI. This, in turn, results in the calculation of an inflated calculation for the assessment amount.

Reasons for Board's Decision:

[32] The Board accepts that the subject is correctly classified as being a Class A- building. This classification is supported by the rent roll submitted to the Respondent by the Complainant and is particularly true when one removes those leases signed by Weatherford Canada Partnership negotiated on July 1, 1999 (Exhibit R-1, page 64) at rates ranging from \$17.00 to \$40.00 per square foot.

[33] Recent leases signed in 2012 and 2013 reflect values in the \$32.00 per square foot range. This supports the Respondent's use of \$30.00 per square foot in their Pro Forma (Exhibit R-1, page 63).

[34] The Board places considerable weight upon the Respondent's Office Rental Analysis for Class A- buildings in the downtown core. A summary of these rates supports the assessment of the subject property which sets the rental rate at \$30.00 per square foot.

[35] The Board places a great deal of weight on the rental rates in Class B buildings provided by the Respondent for the downtown sector of the City. These rental rates fall considerably below those garnered by Class A- buildings and below the current rental rates established for the subject.

[36] As for the argument dealing with capitalization rates, the Board accepts the Respondent's position that the City's methodology of applying the typical NOI parameters closest to the sale date does have the capacity to establish the subject's current market value.

[37] The Board places little weight upon the Complainant's argument that the subject property should be reclassified from a Class A- building to a Class B building. The basis for the Board's position on this matter comes from the observation that the current rental rates in the subject exceed those found in Class B buildings in the downtown core of the City.

[38] The Board rejects the Complainant's argument that Class B buildings cannot carry capitalization rates that are lower than those found in Class A buildings. The application of a capitalization rate in the income stream of a particular property represents only one variable in determining market value. There are other important considerations such as the application of typical expenses and the sales values per square foot of similar properties.

[39] In contrast, the Board places considerable weight upon the Respondent's submission that capitalization rates can vary so long as the determination of the net operating income applied to a capitalization rate results in the establishment of current market values.

[40] In conclusion, the evidence presented by the Respondent is sufficiently compelling to lead the Board to conclude that the assessment of the subject property is fair and correct and should not be disturbed.

DATED AT THE CITY OF CALGARY THIS 3 DAY OF SEPTEMBER 2014.

per 
S. Kashuba

Presiding Officer

APPENDIX "A"**DOCUMENTS PRESENTED AT THE HEARING
AND CONSIDERED BY THE BOARD:**

| NO. | ITEM |
|----------------|-----------------------------------|
| 1. Exhibit C-1 | Complainant Disclosure |
| 2. Exhibit R-1 | Respondent Disclosure |
| 3. Exhibit C-2 | Complainant's Rebuttal Submission |

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.*