

**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-26.1, Section 460(4).

between:

Altus Group, COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

W. Kipp, Presiding Officer

K. Kelly, Board Member

J. Massey, 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 2010 Assessment Roll as follows:

ROLL NUMBER: 067079285

LOCATION ADDRESS: 701 – 8 Avenue SE, Calgary AB

HEARING NUMBER: 59534

ASSESSMENT: \$414,830,000

This complaint was heard on the 7th, 8th, 9th and 10th days of September, 2010 at the office of the Assessment Review Board located at Floor Number 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 7.

Appeared on behalf of the Complainant:

- B. Brazzell, D. Hamilton, D. Genereux, G. Worsley

Appeared on behalf of the Respondent:

- W. Krysinski, A. Czechowskyj

Background:

The subject property, Western Canadian Place, is one of several Class A-AA office buildings in the downtown core where there are complaints against the 2010 assessments. Hearings commenced in June 2010 and continued into July and August. For various hearings, there were different Composite Assessment Review Board (CARB) panels that heard and decided on evidence. Decisions were rendered following some of the earlier hearings.

The Complainant's evidence pertained to a number of issues that were common to all of the Class A and AA property complaints. This evidence had been fully presented and responded to at each prior hearing because of the different compositions of CARB panels.

At this current hearing, the current CARB panel heard a summary of the common issue evidence (see below) and detailed evidence pertaining to the subject Western Canadian Place property. This hearing had been scheduled for the noted four days which was insufficient time to hear evidence for all remaining Class A and AA properties. It was decided that additional hearing time would be allocated as soon as possible for the same CARB panel to hear the remaining complaints. This would eliminate the need for common issue evidence to be heard again when the hearing continues.

On the morning of September 10, 2010, a summary of this decision was orally presented to the parties. This written decision provides full reasoning which led to the conclusions reached by the CARB.

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

As a preliminary matter, the Respondent raised the matter of common issue evidence being heard again at this hearing when it had been presented and responded to at prior hearings. Other CARB panels had heard evidence and argument and made decisions regarding the common issues and it would be frivolous to rehear all of that evidence again at this hearing. The Respondent pointed out that this is not a rehearing. It is a continuation of prior hearings.

The Complainant confirmed that a rehearing was not being requested. After receiving decisions that were issued by prior CARB panels, the Complainant had changed the focus of some of its evidence in response to those decisions. It was the Complainant's position that there was limited precedential value to those prior decisions. This CARB was expected to decide the issues on the basis of the evidence that would be put forward at this hearing.

During the Complainant's argument, it had been suggested that there was additional evidence, updated submissions and different arguments for this hearing. The Respondent was not aware of any evidence changes from prior hearings. The Complainant had filed the new material within the seven day period required for filing of rebuttal evidence.

There was ongoing discussion about the nature of the evidence filed by the Complainant as rebuttal evidence.

Board's Decision:

Having heard all of the argument from both parties, the Board recessed the hearing until the afternoon of September 7th. The current CARB panel comprised two members who had sat on prior panels regarding Class A and AA properties and those members had heard all of the details regarding the common issues being raised by the Complainant. It was only the Presiding Officer who had not previously heard all of the evidence and argument. The recess was to allow the Presiding Officer time to review all materials at hand in order to avoid a lengthy presentation of evidence and argument that had already been heard by other panels including two members of the current panel.

When the hearing resumed at 2:00 PM, the parties were informed that the Presiding Officer had reviewed the evidence as well as prior CARB decisions. It would therefore not be necessary for the parties to present all of their common issue evidence in detail. The parties were informed that all issues should still be addressed but not necessarily in the same detailed manner as at prior hearings.

With respect to the argument about new evidence/rebuttal evidence, the Board decision was to deal with specific issues as they came up rather than to attempt to examine each disclosure document prior to their presentation.

Property Description:

The property that is the subject of this assessment complaint is a two building office complex known as Western Canadian Place, located in the downtown core of Calgary at 701 – 8 Avenue SW. For assessment purposes, the City designates the location as Downtown 2 (DT2). The 41 and 31 storey office towers are above a three level retail podium. There is underground parking for 153 vehicles. In all, there is approximately 55,000 square feet of retail space and 1,050,000 square feet of office space (one of the issues of the property assessment complaint was the amount of floor area so the areas shown here are approximations). Included in the retail floor area are a conference centre on the third retail level and a fitness centre on the basement level. The complex was completed in 1983. There are +15 connections to First Alberta Place, an office building located immediately to the west and across 6 Street SW to the adjacent 635 – 8 Avenue SW office building and Centennial Parkade, a City of Calgary parking structure. Another pedestrian bridge passes over 9 Avenue SW to surface parking lots that are along the south side of 9 Avenue.

Issues:

The Complainant raised the following matters in section 4 of the complaint form:
Assessment amount (No. 3 on the form) and Assessment class (No. 4 on the form).

The Complainant also raised the following specific issues in section 5 of the Complaint form:

- *The subject property is assessed in contravention of Section 293 of the Municipal Government Act and Alberta Regulation 220/2004.*
- *The use, quality, and physical condition attributed by the municipality to the subject property is incorrect, inequitable and does not satisfy the requirement of Section 289(2) of the Municipal Government Act.*
- *The assessed value should be reduced to the lower of market value or equitable value based on numerous decisions of Canadian Courts.*
- *The assessment of the subject property is in excess of its market value for assessment purposes.*
- *The assessment of the subject is not fair and equitable considering the assessed value and assessment classification of comparable properties.*
- *The classification of the subject premise is neither fair, equitable or correct*
- *The information requested from the municipality pursuant to Section 299 or 300 of the Municipal Government Act was not provided.*
- *The municipality has failed to recognize the tax-exempt status of one or more tenants, of the subject property, based on definitions outlined in Section 362 and 364 of the Municipal Government Act*
- *This Notice is filed based on information contained in the Assessment Notice as well as preliminary observations and information from other sources. Therefore the requested assessment is preliminary in nature and may change.*
- *Account for a variety of risk factors the capitalization rate should be increased to 8%*
- *The assessed rental rate applied to the subject property should be \$27.00*
- *The assessed vacancy allowance applied to the subject property should be increased to 8%*
- *The assessment has neglected to account for various elements of obsolescence.*
- *The assessed operating cost allowance applied to the subject property should be increased.*

The same list of issues was included in the Complainant's evidence brief (Exhibit C3) for the subject property.

In the brief that dealt with common issues for Class A and Class AA office properties (Exhibit C2), there was another list of issues:

| | |
|------------------|---|
| <i>Issue #1</i> | <i>Non-compliance with MGA 299 & 300</i> |
| <i>Issue #2</i> | <i>Non-compliance with MGA 293 (fairness & equity)</i> |
| <i>Issue #2A</i> | <i>Selective Reassessment</i> |
| <i>Issue #2B</i> | <i>Inequities Compared to Sale Prices and Other Assessments</i> |
| <i>Issue #2C</i> | <i>Incorrect classification practice</i> |
| <i>Issue #2D</i> | <i>Incorrect & Inequitable Market Analysis</i> |
| <i>Issue #3</i> | <i>Incorrect Income Approach Calculations and Assumptions</i> |
| <i>Issue #3A</i> | <i>Vacancy & Credit Loss Allowance is Too Low</i> |
| <i>Issue #3B</i> | <i>Assessed Rent is Too High</i> |
| <i>Issue #3C</i> | <i>Incorrect Capitalization Rate</i> |
| <i>Issue #3D</i> | <i>Capital Costs, Brokerage Commissions & Short-life Issues</i> |
| <i>Issue #4</i> | <i>Site Specific Issues</i> |

At the hearing, the Complainant stated that the focus would be on Issues #3, #3A, #3B and #3C. Issue #3B would include argument for a reduction of the office space rental rate and a reduction of the rental rate applied to a portion of the retail space occupied by the fitness centre. In addition, the assessable floor area was to be raised as an issue.

Complainant's Final Requested Value:

\$325,360,000 if office rent rate is reduced from \$30 to \$24 per square foot, or alternatively,
\$372,020,000 if the vacancy rate is increased from 3% to 8%, or alternatively,
\$379,320,000 if the capitalization rate is increased from 7.5% to 8.0%.

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

At prior hearings regarding complaints against assessments of Class A and Class AA office building properties, the Complainant had argued that all three elements of the income approach – rent rate, vacancy allowance and capitalization rate – should be adjusted. After reviewing CARB decisions issued regarding those properties, the Complainant came to the conclusion that not all three elements needed to be adjusted. A fair and reasonable assessment would result if any one of the three elements was properly adjusted. If the rental rate was to be set at a more realistic \$24 per square foot (for office space), then there would not be any higher vacancy so the 3% allowance would suffice. Further, at that lower rent, the market would accept a 7.5% capitalization rate as being reasonable. For this reason, the Complainant's requested assessment varies depending upon which of the input factors is changed.

For this hearing, the Board addresses the issues as follows:

1. Office Rental Rate
2. Vacancy allowance
3. Capitalization rate
4. Other

1. Office Rental Rate:

The assessment is based on rental rates of \$30 per square foot for office space, \$10 for recreational space (fitness centre), \$24 and \$21 for retail space and \$12 for cafeteria and storage space.

The Complainant requests that the office rent rate be reduced to \$24 per square foot and that the fitness centre rate be reduced to \$0.

A point of contention was in regard to rent comparables. The Complainant used rent comparables from a number of Class A buildings with no regard to the zone in which the buildings were located. Lease commencement dates were as far back as November 2008 and as far into the future as September 2013. The Complainant considered the date of signing of the lease agreement as being more appropriate for determining market expectations. These dates were as far back as April 2008 and as recent as February 2010. Rental rates, after consideration of periods of rent free occupancy, ranged from \$16.57 to \$42 per square foot. The median rate was \$24.00 and the weighted mean was \$23.67. Data on 41 lease deals was included in the analysis. It was this analysis that formed

the basis of the requested rental rate of \$24 per square foot for office space. There was no complaint regarding the rental rates on other space types, however, lease documents indicated that there was no storage space rented in the building (the assessment included 7,086 square feet of storage space at \$12 per square foot) and it was requested that the assessment on storage space be eliminated entirely.

The Complainant argued that the 18,460 square foot recreational space (the fitness centre) should have a \$0 rent rate. Firstly, this space is amenity space for tenants within the building. Secondly, the landlord does not charge any rent for this space. Any profit received by the landlord from the operation of the fitness club goes to reducing operating expenses. Letters from the subject property manager as well as from other property managers confirmed that several buildings with fitness centres do not charge rent for the space occupied by the fitness centre. In others, there was a small amount of rent charged.

The Respondent based the \$30 office rental rate on a rent study. Only office rent was supported in the evidence because that was the only rental rate being challenged by the Complainant. A table containing details on 53 lease transactions in several Class A office buildings was presented. This data had been extracted from ARFI's (Assessment Request for Information) that had been returned by Class A building property managers. There was no regard given to the downtown zone in which buildings were located, however, it was shown that the \$30 rental rate formed the basis of assessments of Class A buildings in all zones (it is noted that Class A- buildings were accorded a rate of \$28 per square foot). The Respondent considered the lease commencement date as the pertinent date for its analysis, partly because that date is verifiable whereas negotiation dates cannot always be pinpointed. Lease commencement dates were as far back as July 2008 and as recent as July 2009. Lease rates ranged from a low of \$14.00 to a high of \$45 per square foot. The weighted mean of all data was \$33.12 and for lease areas greater than 10,000 square feet, it was \$31.77. Additional support for the selected \$30 rate was in the form of data from industry surveys for the 2nd quarter of 2009. Three industry analysts' surveys indicated rental rates of \$30, \$30 and \$35.19 per square foot.

In rebuttal, the Complainant provided additional data on the lease transactions used by the Respondent. This data was intended to show the relevance and/or accuracy of the Respondent's lease comparables. From clients, the Complainant obtained information regarding the dates of lease negotiation or finalization, whether the leased space was additional space rented by an existing tenant, whether the lease rate reported was the result of a step-up or escalation in an older lease, whether the lease involved a subtenant or whether or not there were tenant inducements. The Complainant concluded that only five of the 53 reported lease transactions were useful in the determination of an office rent rate for the subject. The five useful leases indicated median and weighted mean rates of \$18.50 and \$25.07, respectively.

The Respondent's analysis of the Complainant's lease data concluded that just five of those lease transactions occurred within the relevant time frame leading up to the July 1, 2009 valuation date. These five transactions produced a weighted mean of \$32.84 per square foot.

In its rebuttal, the Complainant had provided a table that combined the lease transactions from the evidence of both parties. About 30 transactions were included and the median and weighted average rates were \$24.50 and \$24.11 per square foot, respectively. The Respondent's analysis of this table concluded that only 12 of the transactions were within the relevant time frame and the weighted mean of those rates was \$30.94 per square foot.

In closing, the Complainant argued that if the Board does not accept the \$24 rent rate indicated by

lease comparables, then it should consider a rate of \$28 per square foot as is applied to two other Class A buildings – Nexen Building at 7 Avenue and 8 Street SW and Plains Midstream Plaza at 8 Avenue and 5 Street SW. The Respondent has both of these properties designated as Class A-properties and \$28 is the rent rate applied to A- buildings. Location, size and other factors went into the designation application.

Board Findings on Office Rental Rate Issue:

The office rental rate for the subject Class A building is \$30 per square foot.

A number of 2010 Calgary CARB decisions have dealt with this matter and those decisions upheld the rate used by the assessor. This Board accepts the Complainant's analysis that shows that some of the Respondent's lease transactions may have been flawed to some extent, however, the majority of the transactions have value in the rent rate analysis and they support the \$30 per square foot rate.

This Board finds that leases that do not commence until after the effective valuation date are of minimal value in the analysis. Leases that were negotiated or that came into effect around the valuation date would have been negotiated between informed parties who were cognizant of the market situation at the time and who would have had an eye to the future as well. A rent rate negotiated and set in June 2009 for a lease commencement date in September 2013 cannot be said to be a 2009 rent rate. For leases where negotiation dates were relatively close to the commencement dates, that data can be relied upon to a greater extent as long as it is not too far beyond the effective valuation date. For the Respondent's transactions nearest the valuation date, the Board finds support for a rate of \$31. With further support from industry reports, the \$30 rate used in making the assessment is reasonable and realistic. Rental evidence was examined from a number of perspectives and in each case, the \$30 rental rate was supported. Within the subject property, one 2009 lease set the rental rate at \$40 per square foot. The Respondent's \$30 based assessment indicates to this Board that the changing market was being recognized.

While differences between Class A and Class A- buildings may be subtle, the Board accepts the Respondent's explanation of the reasons for the subject not fitting into the A- class wherein it would be assessed using a \$28 per square foot rate on office space.

2. Vacancy Allowance:

The Complainant did not undertake a vacancy study. Graphs showing changes in vacancy rates over time were provided. These graphs were based on reported survey results by two analysts – Colliers International and Cresa Partners. Tables of data from which the graphical presentations were derived were from the same sources. For headlease space, Colliers reported a vacancy rate of 4.76% at the end of the 2nd quarter of 2009 while Cresa reported a 1.88% vacancy rate. By the end of the 3rd quarter, the Colliers rate was up to 8.19% while Cresa's rate was 3.11%. There was no explanation for the wide discrepancy in vacancies between these two analysts. For the subject assessment analysis, the Complainant placed most weight on the 3rd Quarter survey data. Part of the rationale for relying on 3rd quarter 2009 data was that July 1 is actually in the 3rd quarter of the year.

The Complainant also relied upon publicly available reports regarding a number of new buildings

that were under construction and that, when completed, would add to the inventory of office space. It was argued that the coming-on-stream of this new space would significantly impact overall vacancy in Class A buildings.

The Respondent had conducted a vacancy analysis from data provided by property managers in ARFI's. That data would have been, for the most part, applicable to March or April of 2009. The study indicated a vacancy rate of 2.389%. Industry survey reports from Cresa, Avison Young, Colliers and Barclay reported vacancy rates of 1.88%, 1.90%, 1.80% and 2.04% respectively for Class A office space at the end of the 2nd quarter of 2009. Based on the vacancy analysis and supportive industry survey data, the Respondent set the Class A office building stabilized vacancy rate at 3.0% which accounted for the market indications that vacancies were increasing.

Board Findings on the Vacancy Rate Issue:

The issue of vacancy rates has been dealt with in several 2010 Calgary ARB decisions where the evidence was the same as is before this Board.

This Board finds that there is no new evidence or argument that would bring about a different decision than was rendered by those other boards.

Technically, July 1 is the first day of the 3rd quarter of the year but third quarter survey results cannot be compiled and studied until the quarter ends and that is after the 30th of September – three months (less one day) after the effective valuation day.

The Respondent found a vacancy of 2.389% which was supported by four industry surveys all showing 2 percent or lower rates. The City used 3.0% in the assessment, stating that the increase from survey results took into account the potential increases in vacancies.

This Board finds that the Respondent's evidence and argument regarding vacancy is most compelling. While there was much speculation about significant increases as new office space came on stream in the short term future, that was just speculation and it had been known for several years that significant blocks of new space were coming on stream. There was no evidence before this Board that showed that the market was reacting in a negative way in making value decisions in 2007 or 2008 when it was known that all of this new space was coming.

3. Capitalization Rate:

The Complainant analyzed three office building sales where some income information was known. Two of the sales occurred in late 2007 and the third closed in February 2010. There was controversy about the reliability of the Court Ordered 2010 sale. When the post-facto sale date was also considered, the Board chose to disregard it entirely. The other two sales provided 2007 capitalization rates of 7.69% (Gulf Canada Square) and 8.03% (Plains Midstream).

The Respondent did not rely on any office property sales because there were no sales within a reasonable period of time leading up to the valuation date. Instead, an overall view of the market was undertaken. It could be confirmed that rental rates had declined, vacancy rates had increased, operating costs had increased and land values had declined. Together, all of this led the Respondent to conclude that capitalization rates would reasonably have increased proportionately to

those other market changes. Based on historical capitalization rates, the Respondent found that a 7.5% capitalization rate would be reasonable for the subject Class A office.

Board Findings on the Capitalization Rate Issue:

This Board has concerns over the Complainant's reliance on two 2007 sales. For one of the sales, Gulf Canada Square, there is disagreement over its classification – the Complainant maintains that it is a Class A property while the Respondent rates it as Class B. For capitalization rate applicability, that does not matter a lot but for rent rate applications, it does. The Complainant maintains that it is an A building with a market rent rate at the time of sale of \$30 per square foot for office space. For the 2007 assessment (the same year as the sale date), the City had used a \$30 rent rate as well. The Complainant's calculated capitalization rate is 7.69%. The Respondent, while admittedly not relying on any sales for its capitalization rate selection, had analyzed the Gulf Canada Square sale from a couple of perspectives and had determined capitalization rates from 5.28% and 6.7%.

For the second sale, Plains Midstream building, the Complainant determined that the market rent rate (in 2007) was \$28 and it reported that the assessment that year had been based on a \$26 rate. At \$28, the capitalization rate was found by the Complainant to be 8.03%. The Board notes that the rate would have been lower had the \$26 rent rate been used. The Respondent's analysis indicated capitalization rates of 7.19% and 7.44%.

This capitalization rate matter has been considered in prior 2010 Calgary ARB decisions. This Board concurs with those decisions in that the most realistic, best reasoned capitalization rate is 7.5%.

4. Other Issues:

Fitness Centre:

The Complainant maintains that the fitness centre space is an amenity to the subject property. There is no rent paid for the club space and the rents for office space in the property compensate for the \$0 fitness centre rent. The Respondent provided evidence to show that the fitness centre was not being operated solely for employees of tenants in the offices. This Board finds that the current assessment of this space is reasonable. This landlord may not charge rent but others could. The Complainant states that any profits from the operation of the fitness club are used to reduce operating costs. There was no explanation provided to the Board as to how the landlord obtained profits from a club it does not own or operate and for which it gets no rent. Further, there was no evidence in the rent comparables to show that rents in the subject were higher than rents in buildings with no fitness club. The Respondent has applied a \$10 rent rate to this lower level space while main and upper floor retail space is allocated rents of \$23 and \$21. Based on information available to the Board, this relationship appears to be reasonable. The fitness centre space is space that could be rented for retail use. Other landlords may very well do that.

Rentable Floor Area:

The Complainant had conducted a review of the subject property rent rolls and determined that there was less office space than was reflected in the assessment. Further, there were minor discrepancies in retail areas and there was no storage space at all. The Respondent undertook to conduct a similar review of rent rolls and came to somewhat similar conclusions. The assessment

was recalculated based on the newly determined floor areas and it was truncated to \$406,960,000. The new calculations were presented to the Board and to the Complainant. The Complainant considered the recalculation to adequately cover its concerns over area measurement. The Respondent opined that the change in assessment calculations was only about two percent of the original assessment and therefore, the assessment should not be changed.

As was explained to the parties at the hearing, the Board is concerned that matters such as disagreements over floor area should be brought forward as issues at an assessment complaint hearing. If there is an error, it can be fixed, either during the early inquiry/consultation period or at any other time by amending the assessment.

The Board does not accept the Respondent's opinion that the assessment should not be altered because the reduction would be one of only about two percent. This two percent reduction amounts to almost \$8 million and that, in the minds of the Board members, is significant. It is a correction of an error. Further, the Board is not bound by any rules regarding the quantum of an assessment change. If it is deemed to be appropriate, the Board can alter any assessment by any percent rate it finds is supported.

This Board will reduce the 2010 assessment of Western Canadian Place to \$406,960,000 to correct the area measurement error.

Board's Decision:

The 2010 assessment of this property is reduced to \$406,960,000 based on recalculation using a more realistic floor area measurement. This includes removal of any assessment on storage space.

The Board will not make any alterations to any of the rent rates, vacancy rates or the capitalization rate.

DATED AT THE CITY OF CALGARY THIS 27 DAY OF SEPTEMBER 2010.



W. Kipp
Presiding Officer

SUMMARY OF EXHIBITS

Exhibit

| | |
|----|--|
| C1 | Assessment Review Board Complaint Form |
| C2 | Complainant's Submission Regarding Class A and Class AA Office Buildings |
| C3 | Complainant's Submission Regarding 701 – 8 Avenue SW |
| C4 | Complainant's Response to City of Calgary Rental Rate Analysis |
| R1 | Respondent's Assessment Brief For 701 – 8 Avenue SW |
| R2 | Respondent's Recalculation of Assessment based on Revised Floor Area |
| R3 | Respondent's Summary of analysis of Five Complainant rent comparables |
| R4 | Respondent's summary of analysis of 12 rent comparables |

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.*