

**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:

4087836 Canada Inc., Brookfield Properties (Bankers Hall) Ltd. (as represented by Altus Group Ltd.), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

***C. McEwen, PRESIDING OFFICER
B. Jerchel, MEMBER
R. Deschaine, 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 2011 Assessment Roll as follows:

ROLL NUMBER: 068108794

LOCATION ADDRESS: 855 2 ST SW

HEARING NUMBER: 63294

ASSESSMENT: \$808,290,000

This complaint was heard on the 19th day of July, 2011 at the office of the Assessment Review Board located at Floor Number 3, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 11.

Appeared on behalf of the Complainant:

- D. Chabot
- G. Kerslake

Appeared on behalf of the Respondent:

- A. Czechowskyj
- D. Lingren

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

1. A preliminary issue filed by the Respondent on July 4, 2011 was formally withdrawn by the Respondent at the outset of the hearing.
2. The Complainant raised a preliminary issue regarding the acceptability of the Respondent's Summary of Testimonial Evidence (the summary). The Complainant stated that the summary did not fully comply with section 8(2)(b) of the Matters Relating to Assessment Complaints (MRAC) insofar as the Respondent's summary did not provide the Complainant sufficient clarity to allow the Complainant to respond fully to the evidence at the hearing.

The Respondent argued that the Complainant was well aware of the evidence within the Respondent's disclosure and that the summary supported the evidence therein and met the requirements of MRAC.

The Complainant again argued the right to know how the Respondent's evidence would be used and that fairness required there be no loose ends. The Complainant provided three specific examples of the deficiencies within the summary:

- Of what relevance is the Court of Queen's Bench Originating Notice (R1, pages 139-142)
- Why is the RealNet Report (R1, pages 194-197) on the sale of the property located at 508, 15th AVE SW included in the disclosure?
- Of what relevance is the sales information (R1, pages 202-233)?

The Respondent replied that two pieces of evidence referenced by the Complainant had been included within the Respondent's disclosure (R1) in error and asked that pages 139-142 and pages 194-197 be removed from the evidence package. The Respondent further stated that the sales information disclosed on pages 202-233 of R1 was referenced in the Respondent's summary (R1, item 11, page 20) as evidence to challenge the Complainant's requested assessment amount.

The Complainant again expressed dissatisfaction with the Respondent's summary and asked that the hearing be postponed until the Respondent resubmitted a summary that fully complied with MRAC.

The Board agreed to strike the irrelevant evidence from the Respondent's evidence

package. The Board found, however, that the Respondent's summary met both the expectations of the Board and the intention MRAC section 8(2)(b)(i) which states:

(b) *The respondent must, at least 14 days before the hearing date,*

(i) disclose to the complainant and the composite assessment review board the documentary evidence, a summary of the testimonial evidence, including a signed witness report for each witness, and any written argument that the respondent intends to present at the hearing in sufficient detail to allow the complainant to respond to or rebut the evidence at the hearing ...

The Board did not interpret MRAC as instruction to either party to provide a summary of such length and detail that the relevance and standing of every particulate of disclosure evidence is established. The Board found that MRAC actually speaks to the entirety of disclosure including the summary, table of contents, witness statements, written argument and evidence. The Board, therefore, found the Complainant's expectation that the Summary of Testimonial Evidence provide the level of detail demanded by the Complainant to be both unrealistic and unreasonable and so, rejects the Complainant's request.

The Board did not accept the Complainant's argument that misplaced evidence should necessarily void a Summary of Testimonial Evidence and, although the Board accepts the right of either party to challenge the accuracy, meaning and relevance of submitted evidence, challenging the summary was not found to be the most appropriate manner of doing so.

The Respondent's Summary of Testimonial Evidence was accepted and the merit hearing continued.

3. Due to time constraints, both parties proposed a postponement of the merit hearing for one day until Tuesday, July 19 at 9am, Boardroom 11. The Board accepted both party's position that the merit hearing would require a least one full day and so, granted the postponement.

Property Description:

The subject property is Bankers Hall, a 2.2 acre site located in Calgary's downtown core (DT1). The site is improved with two towers (Bankers Hall East and West) that provide 1,842,871 square feet of net rentable area comprised of 1,606,504 square feet of office, 193,660 square feet of retail located primarily on the first four floors of the Bankers Hall East Tower and 42,123 square feet of storage. The improvement is classified as AA for assessment purposes.

Issues:

Is the subject property assessed higher than market value and is it, therefore, inequitable with similar properties? Specifically,

1. Should the rental rate on the second floor (500-1500 square feet) be reduced to \$60 per square foot?
2. Should the cap rate be increased to 7%?
3. Should the office rent be reduced to \$27 per square foot?

Complainant's Requested Value:

\$711,300,000

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

1. Should the retail rental rate on the second floor (500-1500 square feet) be reduced to \$60 per square foot?

The Complainant provided a chart showing two recent, second floor leases that indicated lease rates of \$42 and \$70 per square foot. The Complainant argued that the actual rates were a more reliable indicator of market value than the typical rate of \$90 per square foot assessed by the city. The Complainant asked that the subject rate be reduced to \$60 per square foot based upon the median value of the two actual leases provided.

The Respondent argued that the application of the typical rate to the subject spaces reflected both the smaller footprint of these spaces and the higher traffic pattern provided by their Plus15 locations. The Respondent asked that little weight be given the lease information due to the limited number of leases provided and the absence of the lease details.

The Board finds the assessed rate of \$90 per square foot to be correct in the absence of any compelling evidence to change it. The Board does find in the Complainant's submission (C3, page 52), a rent roll showing the two new retail leases provided by the Complainant. The lease for Unit 295 at \$42 per square foot is a lease renewal for a major tenant of Bankers Hall. The lease for Unit 212 is a new lease at \$70 per square foot, but with rapid increases that drive the rent rate to \$100 per square foot by December, 2014. The lease renewal is given little weight by the Board and the new lease, containing aggressive step ups, is found to be somewhat supportive of the assessed rate.

Without further evidence, including valid equity comparables, the Board finds that neither a market nor equity argument exists and so, confirms the rental rate as assessed.

2. Should the cap rate be increased to 7%?

The Complainant submitted that AA office buildings in downtown Calgary are assessed using a standard 7.0% cap rate. There are two exceptions: the subject property, Bankers Hall and an adjacent tower, TD Canada Trust / Eaton Centre, which were assessed using a 6.75% cap rate. The Complainant argued that the lower cap rate on Bankers Hall was arbitrary, unjustified and inequitable relative to all other AA office buildings in downtown Calgary. The cap rate was arbitrary because it was not derived mathematically using actual sales data, unjustified because the retail component within Bankers Hall (the basis of the cap rate premium) contributed such a small segment of the subject's Net Rentable Area (7%) and Net Operating Income (10%) and inequitable because the lower cap rate disadvantaged the subject relative to its peers who compete for customers within the same marketplace. The Complainant questioned the fairness of an assessment that burdens 93% of a property based on the small contribution of the residual space. The Complainant submitted that if the cap rate premium was justified at all, was it not more reasonable to apply it to the retail segment alone?

The Complainant argued that the .25% cap rate premium has been in place for only two years.

Prior to that, downtown AA space had been assessed at the same cap rate equitably. What changed two years ago that suddenly made the subject building more valuable than its peers?

The Complainant provided industry analysis that supported a 7.0% cap rate for AA office buildings in Calgary during the second quarter of 2010. The Complainant argued that none of the industry publications recognized the .25% cap rate premium applied to the subject building.

The Complainant also provided a chart showing the Assessed Capitalization Rates for Property Types in Calgary. The Complainant drew the Board's attention to the 6.50% cap rate applied to Group A Regional Shopping Centres and the 7.25% cap rate applied to the Power and Community Shopping Centres. The Complainant argued that if the intention of the city was to recognize the contribution of the subject's retail space on the overall valuation of the subject, then the subject's retail component more closely resembled the Power/Community Centres, which carry a relatively high cap rate, than it does the Group A Shopping Centres which the city used to develop the subject cap rate.

The Respondent confirmed that AA office space in Calgary was assessed using a 7.00% cap rate. The subject property, however, received a cap rate of 6.75% to recognize the atypical mix of office and retail space within the building. The Respondent argued that the subject property was different than other AA buildings and was assessed as such. In support, the Respondent provided a table of AA Class Downtown Office Buildings showing the percentage of retail space to total building space (not including storage) within the AA office buildings. The table indicated eight AA buildings, excluding the subject property and TD Canada Trust / Eaton Centre, showing an average retail to total space percentage of 2.69%. The subject percentage was indicated as 10.76%. The Respondent argued that the subject's significant retail presence enhanced the building's value as it provided a reliable and diversified income stream for the building. The Respondent further argued that the synergy of office and retail helped to support the achievable rent rates of each component, thereby stabilizing the income of the property and reducing its investment risk. The city reduced the cap rate on the subject property by .25% to recognize the lower risk.

The Respondent then addressed the derivation of the .25% reduction. The Respondent argued that the retail component within Bankers Hall acted like a shopping centre based on its overall size of 193,660 square feet located, for the most part, on the first four floors of the east tower. The retail component, it was argued, was effectively greater than that as Bankers Hall and TD Canada Trust / Eaton Centre are linked and form a "retail spine" offering 349,244 square feet of retail within the central core. The combined size and diversification of this retail area, consequently, was treated like a shopping destination comparable to Regional Group A Shopping Centres which were assessed using a 6.50% cap rate. The Respondent argued that as the subject property was neither a pure office building nor a dedicated retail complex, a cap rate somewhere between the two of them was appropriate to recognize the hybrid nature of the building. Consequently, a midway cap rate of 6.75% was used for assessment purposes.

The Complainant responded that treating Bankers Hall retail like Chinook Centre, a Regional Group A Shopping Centre within reasonable proximity to the subject, was absurd as Chinook Centre offered 1,346,111 square feet of rentable space, almost seven times the available space within the subject property. A better comparison, it was argued, would be Power and Community Centres which are comparable in size (~100,000-250,000 square feet) and were assessed using a 7.25% cap rate. The Complainant, again, questioned the fairness of assessing the entire building with a 6.75% cap rate based on the retail component. The

Complainant asked whether it would not be fairer to separate the office and retail components from one another for assessment purposes.

The Board accepts the assessed capitalization rate of 6.75% for the following reasons:

- Bankers Hall is different than typical AA office buildings due to the size of its retail component. Both parties accept that the subject's retail area is four times larger, on average, than other AA buildings.
- Both parties accept the 7.0% cap rate for AA office buildings. Although there are no recent sales of AA buildings to quantifiably support the 7.0% rate, industry reports provide some evidence that this number is sound.
- The Board finds the Respondent's argument regarding the synergy of retail and office within the subject property persuasive. Retail space provides investors an alternative income stream, typically at much higher rates, than office space, and therefore, a level of stability that a pure office building does not enjoy. That stability and consistency should result in a lower risk profile and, therefore a lower cap rate.
- The Board agrees with the Complainant that Bankers Hall is not Chinook Centre. However, the fact that a huge, retail complex is assessed using a 6.50% cap rate indicates the mitigating influence of size and business type (retail) on risk. As Bankers Hall has both size and retail advantages relative to its peers, a lower cap rate seems reasonable. Relative size within a peer group is given more weight than comparisons outside the group.
- The Complainant's recommendation that the subject property be considered more like a Power / Community Centre would have the effect of raising the subject cap rate which, given the reasons above, the Board finds illogical.
- In the absence of recent sales data from either side, the subject cap rate of 6.75% is accepted by the Board as both fair and reasonable.

3. Should the office rent be reduced to \$27 per square foot?

The Complainant argued that the assessed rental rate of \$30 per square foot was too high based upon recent leasing activity in the subject property within the valuation period. In support, the Complainant provided a table of thirteen leases that indicated start dates within four months of the valuation date and with a weighted average of \$25.83 per square foot. In addition, the Complainant provided a table of eleven leases taken from four AA buildings that started within one year of the valuation date. The weighted mean of the leases was \$27 per square foot. The Complainant also provided industry publications that indicated a range of AA asking rental rates between \$22 and \$35 per square foot during the valuation period. The Complainant argued extensively regarding the validity of lease data and the need for any rent rate analysis to consider whether a lease is new or renewed, whether it is for new construction or existing space, whether the lease commencement is recent or dated and identify the date the terms of the lease were actually agreed to (the deal done date). In a rapidly changing (declining) market, it was argued, the done deal and commencement dates should fall within a year of the valuation date.

The Respondent provided a Transfer of Land document dated April 26, 2010 transferring 50% of the subject property between non-arms length affiliated parties for the consideration of \$433,400,000. The Respondent admitted that the transaction was not an actual sale on the open market but that it suggested a subject valuation well above the assessment amount. The Respondent also provided the rent rolls for Bankers Hall West and East which showed rent rate

weighted averages of \$28.51 and \$28.70 per square foot respectively. The Respondent also provided a 2011 Downtown Office AA Class Rental Analysis which showed sixteen leases from six buildings demonstrating a median of \$32 per square foot and a weighted mean of \$32.45 per square foot. In addition, the Respondent provided industry reports that showed the average asking rate for AA space during the valuation period ranged between \$22 and \$35 per square foot. The Respondent argued that the subject property would be on the high end of industry estimates. The Respondent also argued that the Complainant's advancement of the deal done date was purely theoretical and impossible for an assessor to apply in a fair and consistent manner. Such information is highly unreliable, the Respondent argued, because the deal done date is not necessarily captured in any documentation and may vary depending on the interpretation by either party of when the deal done date actually occurred. The Respondent submitted that filtering leases through a deal done date screen was, therefore, unreasonable. The city used the lease commencement date in rent rate analysis because it was legislated, well documented and easily verifiable.

In rebuttal, the Complainant provided a letter from Brookfield Office Properties dated June 6, 2011 stating that the in-house transfer of the subject property on April 26, 2010 should be used with caution for valuation purposes as the transfer amount did not represent a fee simple value of the property. The Complainant also provided three leases within the subject property including a significant lease for Bennett Jones commencing June 1, 2010 at a rate of \$26 per square foot. The Complainant argued that the lease should be considered as new as the original terms of the 1989 lease had expired and the replacement lease fully renegotiated. The Complainant again challenged the city's 2011 AA Rent Rate Analysis on the grounds that the several leases used within the analysis were invalid because they were either construction leases (signed at a higher than typical rate) or negotiated more than a year prior to the lease commencement date and, therefore, unrepresentative of the market conditions prevalent as of the valuation date.

The Board finds the assessed rent rate of \$30 per square foot fair and reasonable for the following reasons:

- The Board accepts the lease commencement date as a consistent and verifiable marker by which to screen lease activity for the purposes of analysis. The Complainant's introduction of a conceptual element, the deal done date, to the pre-qualifying criteria, is found to introduce a level of inconsistency and uncertainty that complicates and, potentially undermines, the assessment process. Although the Board finds the Complainant's argument compelling, that a deal done closest to lease commencement is the best indicator of value, the Board favours the consistency, reliability and verifiability of the lease commencement date used by the Respondent.
- The Board does not accept that construction leases are an invalid indicator of market rent rates as the Complainant's evidence has not sufficiently demonstrated that to be so.
- The Board, therefore, accepts the Respondent's 2011 AA Rent Rate Analysis indicating a median of \$32 per square foot and a weighted mean of \$32.45 per square foot as a better, more inclusive analysis than the Complainant's.
- The Board finds the rent rolls for Bankers Hall West and East which show rent rate weighted averages of \$28.51 and \$28.70 per square foot respectively as supportive of the assessed rate. The subject rent roll indicates that many of the leases are multi-floor leases which reduce the weighted average somewhat.
- The Board gives the Bennett Jones lease little weight as it is found to be a lease renewal. Not only does the lease document describe it as such but the lease continues a

relationship between landlord and tenant that has been in place since 1989.

- The Board gives the Complainant's other two subject leases little weight as both are described as renewals on the subject rent roll.

The Board notes that the subject assessment shows a significant \$74,730,000 reduction from the 2010 assessment, indicative that the city has been responsive to the change in economic conditions. In addition, the Board finds the non arms-length transfer of 50% of the subject property in 2010, suggesting a subject value of \$866,800,000, interesting. Although not definitive, the transfer value is supportive of the subject assessment.

The Board finds the subject assessment both fair and equitable.

Board's Decision:

The assessment is confirmed at \$808,290,000.

DATED AT THE CITY OF CALGARY THIS 10th DAY OF AUGUST 2011.

C. McEwen

C. McEwen
Presiding Officer

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

NO.	ITEM
1. C1	Complainant Preliminary Argument
2. C2	Complainant Disclosure
3. R1	Respondent Disclosure
4. C3	Complainant Rebuttal

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.*