

**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:

***ARTIS MACTRI LTD., COMPLAINANT,
as represented by ALTUS GROUP LIMITED***

and

The City Of Calgary, RESPONDENT

before:

***T. Helgeson, PRESIDING OFFICER
B. Jerchel, MEMBER
J. Kerrison, 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 2012 Assessment Roll as follows:

ROLL NUMBER: 067029199

LOCATION ADDRESS: 800 5th Avenue SW

HEARING NUMBER: 67824

ASSESSMENT: \$68,650,000

This complaint was heard on the 20th day of August, 2012 at the office of the Assessment Review Board located at Floor Number 4, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 2.

Appeared on behalf of the Complainant:

- *M. Meiklejohn*

Appeared on behalf of the Respondent:

- *A. Czechowskyi, L. Gosselin* (in-house legal counsel)

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

[1] At the commencement of the hearing, the Respondent asked that the Complainant be allowed to submit their rebuttal immediately following their submission on the evidence, i.e., that the rebuttal be submitted before the Respondent's submission on the evidence. The Respondent indicated that their legal counsel had consulted legal counsel for the Calgary Assessment Review Board on this issue, and were awaiting a response.

[2] The Board noted that the mandatory hearing procedure provided in s. 37 of the *Calgary Assessment Review Board Policies and Procedural Rules* requires that the rebuttal evidence of a complainant must follow the presentation of the respondent's evidence. This reflects the purpose of the rebuttal, i.e., to rebut the evidence of the Respondent. Until the evidence of the Respondent is put before the Board, there is nothing to rebut. The Board's decision on the Respondent's request is that until advice to the contrary is heard from the Board's counsel, the hearing procedure will conform to s. 37.

Property Description:

[3] Assessed at \$68,650,000, the subject property, known as Trimac House, is a 23 storey office building located at 800 5th Avenue SW in the "DT2" economic zone of downtown Calgary. Constructed in 1982 by Trimac Construction, the subject property has an assessed area of 238,247 sq. ft., of which 4,004 sq. ft. is retail space. As assessed, the subject property has been given a quality rating of class "A-," and the assessment is based on the income approach, with a capitalization rate ("cap rate") of 6.75%.

Issues:

[4] The Board found the determinant issues in this complaint to be as follows:

1. Is the cap rate used in the assessment too low?
2. Does the subject property suffer from a chronic high vacancy rate?
3. Is the assessed rate for parking stalls too high?
4. Are rental rates as assessed for office and retail space too high?

5. What is the correct, fair and equitable assessment for the subject property?

Complainant's Requested Value: \$48,650,000

Summary of the Complainant's Submission

Characteristics and Physical Condition, Municipal Government Act, s.289(2)(a)

[5] As assessed, the characteristics and physical condition of the subject property are incorrect relative to properties comparable to the subject property. When the characteristics and physical condition are not correct, the wrong factors are invariably applied.

[6] It is an accepted concept that for income producing properties, all relevant physical and economic attributes of a property will manifest themselves in the property's capacity to generate income. That said, one must be watchful, for to underestimate or overestimate a property's assessed value for the sole purpose of conforming to a list of subjective (and possibly biased) classifications can result in assessments that do not reflect market values. This can result in erroneous, inequitable assessments, and skewed assessment ratios.

Location and Functionality

[7] The subject property, Trimac House, is located on the corner of 5th Avenue and 7th Street SW, near the eastern boundary of the DT2 economic zone. No differential has been applied for location. The office space is assessed at \$20 per sq. ft., and its retail space at \$24 per sq. ft. Those values should be \$16 per sq. ft., and \$20 per sq. ft., respectively.

[8] The building category is not as important as the functionality of the building. When you move westward in the downtown core, you get into more residential development, and rental rates decrease, as do parking rates. Significantly, the subject property is not connected to the +15.

[9] Leasing in the subject property occurred in 2007 and 2008, before the crash in September of 2008. The most recent lease is at \$16 per sq. ft. That vacancy in the subject is higher than usual is attributable to the age of the building, and the fact that it has no access to +15.

Property Classification, Economic Zones, Rental Rates, and Capitalization Rate

[10] If the benchmark capitalization rate ("cap rate") for "AA" buildings is 6.8%, the cap rate should be higher for an A- building to reflect greater risk. Clearly, the subject property is not comparable to Bankers Hall. The subject property suffers from its location, lack of +15, a small floorplate, and age.

[11] In its assessments of A- buildings, the Respondent does not differentiate between rental rates in A- buildings in DT1, and A- buildings in DT2, but the Respondent does recognize a differential in rental rates between B class buildings in DT1 and B class buildings in DT2. It is submitted that a similar differential must necessarily exist with respect to A- class buildings in DT1 and DT2.

[12] With respect to A- buildings in DT1 generally, full floor tenancies with terms greater than 3 years, show a weighted average of \$20.28 per sq. ft. The Respondent's assessed rate for these buildings is \$22 per sq. ft.

Valuation Parameters and Requested Assessment

[13] In summary, valuation should be based on the characteristics and physical condition of the building. The assessed rate for office space in the subject property should be reduced from \$20 to \$16 per sq. ft., but a rate of \$18 is acceptable. Retail space should be no more than \$20 per sq. ft. The office vacancy rate should be increased from 9% to 10%, and the parking rate reduced from \$475 to \$425, to reflect the difference between DT1 and DT2. Furthermore, the cap rate should be 7.5%, not 6.75%. These adjustments would result in an assessed value of \$48,650,000, or \$203 per sq. ft. of building area.

Summary of the Respondent's Submission

Classification and Post Facto Sales

[14] The subject property has been classed as an A- building since 2007. Board Order 7507 tells us that *post facto* sales help to determine fair market value. The Scotia Centre sale supports a value of \$381 per sq. ft. As assessed, the subject property is valued at \$288 per sq. ft.

Rents, Capitalization Rates, and Assessment-to-Sales Ratios

[15] The Complainant is not contesting the assessment of the subject property as a whole, but bit by bit. The Complainant is asking the Board to adopt a cap rate based on higher rents. In other words, the Complainant is asking the Board to take a cap rate developed from rental rates of \$24 to \$25 per sq. ft., and apply it to rates of \$16 per sq. ft.

[16] Cap rates reported by the industry, i.e., CBRE and Colliers, indicate a cap rate of 6.75 for A class buildings in 2012. Similarly, seven A- class equity comparables in DT2 share this cap rate of 6.75%. Further to this, the recent *post facto* sale of the subject property indicates a cap rate of 6.7%, less than the cap rate of 6.75%, as assessed. The best test of whether the application of a cap rate will produce an assessment that reflects market value is found in the assessment-to-sale ratio ("ASR") of the property in question, and the ASRs of properties comparable to it. To determine the ASR, typical inputs must be used.

Sale of the Subject Property

[17] The subject property sold on May 1st, 2012, for \$100,907,000. Although the sale was *post facto*, it definitely suggests a market value substantially beyond the assessed value. An analysis of downtown A- class rent equity comparables indicates a mean of \$19.67 per sq. ft. The subject property, an A- class building in the west end of downtown, is at \$20 per sq. ft.

Vacancy

[18] As for vacancy, our analysis shows an average vacancy rate of 8.31% for A- buildings in DT2. This is a rate lower than the requested vacancy rate, even though the subject property's

previous vacancy of 17.41% is included in the analysis. Information with respect to the 2012 sale of the subject property indicates a current vacancy of 1.4%. That suggests that the vacancy during the assessment year was due to renovations in anticipation of sale, not a chronic vacancy problem.

Parking Rates

[19] With respect to parking rates, CresaPartners reports rates for A class buildings in the second quarter of 2011 at \$508.43 for reserved stalls, and \$472.92 for unreserved. Parking as assessed for the subject property is \$475 per stall.

Factors to be Considered

[20] If we make enough adjustments, we are bound to come up with a revised assessment. We say look at the recent sale of the subject property. With a time adjustment of 2.27% applied over 11 months, the value is \$76,487,506 for the subject property. The building permits mentioned on page 17 of Exhibit C-1 indicates why the vacancy was 17%; renovations were proceeding in preparation for a sale in 2012. As for the Gulf Canada sale, REIT sales can't be ignored entirely.

Summary of the Complainant's Rebuttal

Economic Zones, Vacancies, and Rents

[21] The Respondent's A- rent survey should have reflected the Respondent's vacancy survey, i.e., the rent survey should have been divided between DT1 and DT2. When vacancies go up, rents go down, and vacancies are higher for A- buildings in DT2 than in DT1. That implies rents will be lower in DT2.

[22] The Respondent did not use or consider leases that commenced after the valuation date of July 1st, 2011. Given the definition of market value and the valuation date of July 1st, *post facto* leases should not be used in assessing property, but using a *post facto* lease or sale to test a valuation is acceptable, provided there is an adjustment for time. The Respondent has presented no time adjustments.

Rent Differentials between Economic Zones

[23] We separated A- buildings into DT1 and DT2, and found the weighted average of rents in DT1 was \$21.48 per sq. ft., and the weighted average of rents in DT2 is \$18.61 per sq. ft. With lease renewals removed from DT2, the weighted average is \$15.96 per sq. ft. Clearly, the latter value supports our request for \$16 per sq. ft. for the subject property.

Sales, Parking, and Capitalization Rates

[24] To be relied upon for assessment purposes, sales should be at arm's length. With respect to the two Scotia Centre sales that occurred in April, 2011, i.e., within the valuation period, the only valid sale is the one for the first 50% interest. It was purchased by Scotiabank from Aspen, and was a straight cash sale. The resulting cap rate is 7.50%. The other Scotia sale is unreliable; Scotiabank lent Homburg (a REIT) the money to make the purchase, and Scotiabank induced the sale. Homburg also got the lucrative management contract.

[25] The sale of Gulf Canada Square occurred on September 2nd, 2011, two months *post facto*. As mentioned above, the general rule is that you do not use *post facto* sales other than for testing an assessment, and only when the sales are time-adjusted.

[26] Included in the Gulf Canada sale was the right to use 240 parking stalls in the adjacent City of Calgary parkade. The Respondent did not use the income from the parking stalls in the assessment of Gulf Canada Square, but had they done so, the cap rate would have been greater than 6.39%. That said, the only valid sale of a Class A building is the one between Scotiabank and Aspen.

Scotia Centre Sale, and Risk

[27] If the income from the two smaller buildings that accommodate businesses, i.e., Mango Shiva and Riley & McCormick, is added to our income approach analysis for Scotia Centre, the resulting cap rate becomes 6.86%. If income from the two smaller buildings is not included, the cap rate becomes 6.73%. Scotia Centre is superior to the subject property, hence has less risk; why should the cap rate for Scotia Centre be roughly the same as the cap rate of the subject property?

Assessment-to-Sales Ratios

[28] There is something inconsistent with respect to how downtown A and AA class buildings, and downtown B and C class buildings are assessed. An analysis of assessment-to-sales ratios for 37 AA, A, B and C class buildings produced a mean ASR of 0.654, and a median ASR of 0.586. For Class AA and A buildings, the mean ASR is 0.979, and the median is also 0.979. This indicates vertical inequity in assessment. This puts Trimac House at a disadvantage with respect to all the B and C buildings in downtown Calgary. The request is to place A- buildings in line with B buildings

Summary

[29] To sum up, when you divide the A- class properties by their economic zones, DT1 and DT2, the typical office rental rate for the subject property turns out to be \$16 per sq. ft., not \$20. Although the Respondent recognizes that there is a difference in vacancy rates between DT1 and DT2, it fails to recognize a difference in rents. During the assessment year, the vacancy in the subject property was 17%. There should also be a difference in the parking rates between DT1 and DT2. Finally, the cap rate should be 7.5%, not 6.75%. These adjustments will solve the inequity, and result in the requested assessment.

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

Sales, Cap Rates, and Vertical Inequity

[30] The Complainant submits that the cap rate of 6.75% for the assessment of the subject property does not adequately reflect its risk as a lesser property when the benchmark for AA buildings is 6.8%. The cap rate should be derived from arm's-length sales, and net operating income. The evidence shows that there were only two sales of an A class office building in DT1 during the agreed-upon valuation period, i.e., the period from July 1st, 2010 to July 1st, 2011. Both sales were of Scotia Centre at 225 7th Avenue SW, and both occurred on the same date, April 21st, 2011.

[31] Each sale was for a 50% interest. In one transaction, the vendor was Aspen Properties, the purchaser Scotiabank, and the sale price was \$95,000,000. At the same time, Scotiabank sold a 50% interest in Scotia Centre to Homburg Canada REIT GP for \$116,000,000.

[32] The Complainant submits that the sale from Scotiabank to Homburg Canada was “bad” because Scotiabank lent Homburg the money for the purchase and brokered the sale, but insists that the sale from Aspen to Scotiabank for \$95,000,000 was a “straight cash” deal, hence a valid sale that supports a non-typical cap rate of 7.40%, and a cap rate (as assessed) of 6.50%. The Respondent agrees with the Complainant as to the Scotiabank to Homburg sale, and submits that the Aspen to Scotiabank sale was not brokered, therefore unreliable as an indicator of fair market value.

[33] Another sale that was considered was one that occurred in September, 2011. This was the sale of Gulf Canada Square, an A class building, which has an assessed cap rate of 6.75%. In addition to being *post facto*, the Respondent’s evidence was that there was a right of first refusal. The Complainant submits that had the parking stalls been included in the assessed value, the cap rate would be more than it is now, thus supporting the Complainant’s argument for a higher cap rate for the subject property. This ignores the fact that the parking stalls are leased from the City of Calgary, and the Board can but wonder how much more the lessee could charge for parking over and above what it is paying the lessor.

[34] The Board finds that the above sales are hardly characteristic of what might be called a universe of sales, and concludes that none of the sales are sufficiently trustworthy to found a valid cap rate. In the absence of substantive evidence, the cap rate used in the assessment of the subject property is confirmed at 6.75%.

[35] Finally, with respect to the Complainant’s argument that there is “vertical inequity” between A class buildings with ASRs approaching 1.00, and B class buildings whose ASRs are in the 0.5 range, the Board agrees that the inequity should be remedied, but not in the manner contemplated by the Complainant, i.e., to reduce the assessments of A buildings so their ASRs would approximate those of B buildings. That would only worsen the problem, and result in further breaches of s. 10(3) of the *Matters Relating to Assessment and Taxation Regulation* (“MRAT”).

Vacancy

[36] Vacancy may be short term, or long term. Generally, higher than normal vacancy must be long term, or “chronic,” before it will be taken into account in an assessment. The Board finds that there is no evidence that the subject property suffers from a chronic high vacancy rate. On the contrary, it appears that renovations were proceeding in the vacant space in anticipation of the sale of the subject property, and by May 1st, 2012, the time of sale, the subject property was very nearly fully leased. Further to this, the evidence indicates that the average vacancy rate for A- buildings in DT2 is 8.31%. The vacancy rates for both office space (0.9%) and retail space (0.7%) will remain as assessed.

Parking

[37] As assessed, the parking rate for the subject is \$475 per stall. The Complainant provided information from a third party, Cresa Partners, in support of a lower parking rate for A- buildings

in DT-2. This information indicates median rate of \$450 per stall for reserved parking, and \$435 for unreserved parking. The Complainant provided no evidence with respect to the number of stalls in the subject property that are reserved and the number that are unreserved. In the result, the Board found insufficient evidence to support an adjustment in the assessed parking rate, and the assessed parking rate is confirmed at \$475 per stall.

Rental Rates

[38] The Complainant submits that rents in A- buildings in DT2 should be less than rents in A-class buildings in DT1. In support of this argument, the Complainant introduced data in tabular form showing office rents of B class buildings in DT1, and in DT2. The average of the rents in DT1 is \$14.77, but in DT2, the average is \$12.39, a difference of \$2.38 per sq. ft.

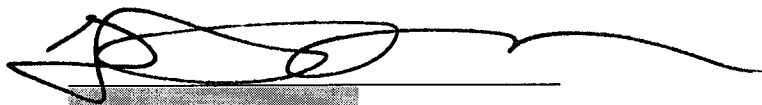
[39] Further to this, a table at pages 15 and 16 of Exhibit "Part I C3A" (part of the Complainant's rebuttal), shows all leases that commenced during the valuation year in A-buildings in DT1 and DT2. The A- leases in DT1 reveal a mean of \$20.66 per sq. ft., and a weighted average of \$21.48 per sq. ft. The mean for the leases in DT2 is \$16.97 per sq. ft., and the weighted average \$18.61 per sq. ft.

[40] The Complainant's evidence demonstrates that there is a significant difference in A- rental rates between DT1 and DT2. In connection with this, the Board notes that just two years ago, the subject property was classified as a B class building.

Board's Decision:

[41] The Board finds, on the evidence, that the appropriate assessed office rental rate for the subject property is \$18 per sq. ft. Based on that \$18 office rental rate rate, with all other factors remaining the same, the assessment is reduced from \$68,650,000 to \$62,460,000.

DATED AT THE CITY OF CALGARY THIS 16 DAY OF October 2012.



Presiding Officer

Exhibits

C-1, Complainant's Evidence Submission

R-1, Respondent's Assessment Brief

C-2, Complainant's Realnet Reports

Part I, C3A, Complainant's Rebuttal Submission

Part II, C3B, Complainant's Rebuttal Submission - Authorities

<u>Appeal type</u>	<u>Property type</u>	<u>Property sub-type</u>	<u>Issue</u>	<u>Sub-issue</u>
CARB	Office	High Rise	Income Approach	Land & Improvement

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.*