

**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:

Western Securities Limited (as represented by Altus Group), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

W. Kipp, PRESIDING OFFICER

G. Milne, MEMBER

J. Pratt, 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: 180077604

LOCATION ADDRESS: 8120 Beddington Boulevard NW, Calgary AB

FILE NUMBER: 67615

ASSESSMENT: \$42,520,000

This complaint was heard on the 29th day of August, 2012 at the office of the Assessment Review Board located at Floor No. 3, 1212 – 31 Avenue NE, Calgary, Alberta, Boardroom 8.

Appeared on behalf of the Complainant:

- *A. Izard & B. Neeson & K. Fong*

Appeared on behalf of the Respondent:

- *B. Thompson & S. Turner*

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

[1] There were several files for community/neighbourhood retail shopping centre properties where Altus Group represented the Complainants. For all of these files, an issue for the Board to decide was the appropriate capitalization rate to be applied in the income approach. Since the issue was the same for all properties, it was agreed by the parties and accepted by the Board that the capitalization rate issue would be argued once (for File 68412) and then it would be carried forward and become applicable to all of the remaining files where the capitalization rate was an issue. This is one of the files where the capitalization rate evidence and argument have been carried forward.

Property Description:

[2] The subject of this complaint is Beddington Towne Centre, a community shopping centre in the Beddington community of northwest Calgary. In all, there are 176,583 square feet of commercial rental unit (CRU), bank, storage, "big box" store, office, pad restaurant and supermarket space. Years of construction of the buildings are 1980 (164,576 square feet), 1991 (6,277 square feet) and 1999 (5,730 square feet). The land component comprises a 14.99 acre site at the northwest corner of Beddington Boulevard and Centre Street NW.

[3] The 2012 assessment of this shopping centre is \$42,520,000 (after an allowance of \$1,050,000 for space occupied by a tax exempt tenant). The buildings are assessed as "B" quality buildings.

Issues:

[4] In the Assessment Review Board Complaint form, filed March 5, 2012, Section 4 – Complaint Information had check marks in box #3 "Assessment amount" and box #4 "Assessment class."

[5] In Section 5 – Reason(s) for Complaint, the Complainant stated several grounds for appeal but not all of these were addressed at the hearing.

[6] At the hearing, the Complainant pursued the following issues:

Is a 7.75% capitalization rate more reflective of the market than a 7.25% rate?

What is the correct rent rate to be applied to "big box 14,001-40,000 square feet" space?

Complainant's Requested Value: \$38,810,000 (Revised at the hearing)

Position of the Complainant:

[7] **Capitalization Rate:** The Complainant argued that the 7.25% capitalization rate used by the assessor in making assessments of community-neighbourhood shopping centres is too low and therefore not reflective of market conditions as at July 1, 2011. It was argued that the Complainant's analysis of sales of shopping centres, which was fully supported by backup documentation, generated a 7.75% capitalization rate which should be applied in making the assessments of neighbourhood-community shopping centres. The "Neighbourhood-Community Shopping Centres – 2012 Capitalization Rate Analysis & Argument – Appendix," entered as Exhibit C3 describes two analysis methods:

Capitalization Rate Method I: The Application of Assessed Income as Prepared by the City of Calgary Assessment Business Unit ('ABU')

and

Capitalization Rate Method II: The Application of Typical Market Income as Prescribed by the Alberta Assessors' Association Valuation Guide ('AAAVG') and Principles of Assessment I for Assessment Review Board Members and Municipal Government Board Members ('Principles of Assessment I')

[8] The Complainant analyzed the sales of seven community shopping centres, using each of the two described capitalization rate derivation methods.

<u>Property</u>	<u>Method I Cap. Rate</u>	<u>Method II Cap. Rate</u>
Pacific Place Mall – 999 – 36 St NE	7.00%	7.63%
Sunridge Sears Centre – 3320 Sunridge Way NE	6.55%	7.40%
Calgary East Retail – 2929 Sunridge Way NE	8.89%	7.81%
Braeside Centre – 1919 Southland Dr SW	8.36%	7.71%
Cranston Market – 356 Cranston Road SE	6.38%	7.34%
McKnight Village Mall - 5220 Falsbridge Gate NE	8.25%	8.03%
Chinook Station Office Depot - 306 Glenmore Tr	8.37%	8.65%
Mean of 7:	7.69%	7.80%
Median of 7	8.25%	7.71%

[9] Method I relates the sale price of the property to the assessed income in the year of the sale. For example, if the sale occurred between January and December 2010, the income used in making the assessment of community centres as at the valuation date of July 1, 2010 would be used. The Complainant maintained that this method is similar to that used by the Respondent in its capitalization rate study.

[10] The valuation date for the current (2012) assessment was July 1, 2011. The seven sales in the Complainant's study had sale dates from January 20, 2009 (29 months prior to the valuation date) to May 27, 2011 (one month prior to the valuation date). Five of the sales occurred in 2009 and two in 2011. There were no community-neighbourhood shopping centre sales during 2010.

[11] Method II uses typical rents as at the sale date to determine the income amount to be put into the direct capitalization formula ($\text{Cap. Rate} = \text{Net Operating Income} / \text{Sale Price}$). The recommendations in the 'AAAVG' were followed:

1. *For most tenants the best source of market rent information is the rent roll. Using these rent rolls, the best evidence of "market" rents are (in order of descending importance):*
 - *Actual leases signed on or around the valuation date,*
 - *Actual leases within the first three years of their term as of the valuation date,*
 - *Current rents for similar types of stores in the same shopping centre,*
 - *Older leases with active overage rent or step-up clauses.*
2. *As a secondary source of rent information, and as a check on the rents derived from the actual rent rolls, the rental rates can be compared to the rents established for similar tenants in other similar properties.*

If comparable information is not available, it may be necessary to analyze the existing lease and interview the owner and tenant(s) to determine what the current rent on the space should be.

[12] Excerpts from the Principles of Assessment I materials were in evidence as were portions of documents produced by The City of Calgary in past years that described the city's capitalization rate extraction method which was similar to that used by the Complainant in this matter.

[13] In the application of Method II, the Complainant examined rent rolls for the individual properties that sold. Rents were also obtained from other properties offering similar space to that in the sale property. "Typical" rent rates were applied in each analysis along with typical vacancy, operating cost and non-recoverable expense rates. The capitalization rates from Method II were not significantly different than those produced in the Method I analysis and all of the mean averages and medians supported the requested 7.75% capitalization rate.

[14] **Rent:** With respect to the rental rate for "big box 14,001-40,000 square feet" space, the Complainant argued that the applicable rent rate should be reduced from \$17.00 to \$14.00 per square foot. Beddington Towne Centre is one of only a few enclosed mall shopping centres in Calgary that is classed and assessed as a community shopping centre. London Drugs, the occupant of 25,989 square feet, is one of the larger tenants in the mall. The London Drugs store is only accessible from the internal mall – there is no outside access or egress.

[15] The London Drugs store is unique and there are few, if any, comparable stores in Calgary. The "mall only" access is a factor, however of more relevance is the additional operating expense that is associated with a mall type shopping centre in comparison to "non-mall" centres. The Respondent has determined that this size category of store has a typical rent rate of \$17.00 per square foot but that rate is based on an analysis of big box stores that are not within enclosed malls. The Complainant provided lease data for one store lease that was considered to be most comparable. That store is a Sport Chek store of 16,650 square feet in Westbrook Mall at Bow Trail and 37 Street SW. This store has similar characteristics to the London Drugs premises in Beddington. A five year lease commenced on this Sport Chek store on June 30, 2011 at a rental rate of \$13.50 per square foot. Effective August 13, 2011, the subject London Drugs lease was renewed at a rental rate of \$14.00 per square foot. This renewal, supported by the Sport Chek lease in Westbrook indicates that \$14.00 per square foot is the proper rent rate for the space.

Position of the Respondent:

[16] **Capitalization Rate:** In its capitalization rate study, the Respondent used property sales that occurred within 24 months of the valuation date and then studied rent rates going back 30 months from that date. The 24 month sale cut-off date eliminates two properties from the capitalization rate study that were contained in the Complainant's study. These two properties are McKnight Village Mall and Chinook Station Office Depot. One sale not used by the Complainant, The Market at Quarry Park (sale in April 2010), was in the Respondent's study.

[17] The six property sales analyzed by the Respondent sold between October 2009 (20 months prior to the effective date of value) and May 2011 (one month prior to the valuation date).

<u>Property</u>	<u>Cap. Rate</u>
Cranston Market - 356 Cranston Road SE	5.29%
Braeside Shopping Centre - 1919 Southland Drive SW	7.10%
Calgary East Retail - 2929 Sunridge Way NE	8.85%
Market at Quarry Park – 163 Quarry Park Blvd SE	5.47%
Sunridge Sears Centre - 3320 Sunridge Way NE	6.55%
Pacific Place – 999 – 36 Street NE	7.00%
Mean average of 6:	6.71%
Median of 6:	6.77%

[18] The Respondent maintained that a “conservative approach” was taken when the capitalization rate for community – neighbourhood shopping centres was set at 7.25% when the mean and median averages of the sales analysis were 6.71% and 6.77%.

[19] In response to the Complainant's comment about their Method I being similar to the analysis method used by the city, the Respondent stated that the city has never used or accepted that method.

[20] It was argued the Complainant's analysis of the Braeside sale was incorrect because it contained a mix of input variables. In prior years, the city had classified Braeside as a “strip” retail centre. In 2010, the classification was changed to “community” centre. It was argued that the Complainant analyzed the sale by using “strip” centre rates but “community” centre vacancy, operating cost and non-recoverable expense rates. This inconsistency generated an incorrect capitalization rate.

[21] The analysis of the Cranston Market sale had been complicated by the fact that this was a new shopping centre. For the first year that it was assessed, there was minimal income data available so it was rated as an A- quality centre. In the next year, when income and sales information was made available, the class was raised to A+. In one capitalization rate analysis, A+ inputs were used while A- inputs were input at other times. Exhibit R1 showed the Respondent's capitalization rate extraction was related mostly to A+ income amounts.

[22] The Market at Quarry Park, in the opinion of the Respondent, was a legitimate sale and thus it is included in the capitalization rate analysis. The Respondent did offer that in other assessment complaint hearings, some CARB's have accepted it and some have rejected it. If this sale is removed from the analysis, the mean and median rates still support the 7.25% capitalization rate.

[23] The Complainant's Method II was criticized as being a mix of actual rents and typical rents in the income analyses. In some cases, only a single rent comparable was used as the basis for a typical rent rate. That is not an accepted mass appraisal procedure. In other cases, rents were used that came from leases that did not commence until after the valuation date. Further, the AA AVG relied upon by the Complainant is not a mandated process to be used in capitalization rate analysis – it is merely a guideline.

[24] In response to criticism from the Complainant about there being several variants of the capitalization rate study produced by the city, the Respondent maintained that errors had been corrected from time to time but the basis of the study had not been altered. In each version of the study, the conclusions always lead to a 7.25% capitalization rate.

[25] The Respondent finds typical rent rates for various types of space in the returns from owners in response to Assessment Request For Information (ARFI) forms that are sent to all property owners or managers each year. Lease transactions that occurred within a 30 month period prior to the valuation date are used. For some more common types of rental space, rent rates for just the subject city quadrant are used. For space types that are more limited in supply (i.e., supermarkets, banks, theatres), a city-wide approach is taken. If a sale occurred in 2010, then typical rents as at the July 1, 2010 valuation date (for the 2011 assessment) were used.

[26] Assessment to sales ratios (ASR's) were calculated for each of the sale properties using the capitalization rates found by each of the parties. These ASR's require the application of a time adjustment to historic sale prices and some data was provided in the Respondent's evidence (Exhibit R1) to support the time adjusted prices. The analysis showed that the 7.25% capitalization rate used by the Respondent produced ASR's that were more within the acceptable range (0.950 to 1.050) than when a 7.75% capitalization rate was used.

[27] **Rent:** The Respondent questioned whether the London Drugs lease was actually renewed in 2011 or whether the \$14.00 rate was merely a step-up in an older lease. Referring to the 2011 Assessment Request For Information (ARFI) return for Beddington Towne Centre, the London Drugs lease commencement date was in 1996. No 2011 date was shown.

[28] As can be seen on the subject property assessment detail report, enclosed malls are given a higher operating cost allowance (\$21.00 per square foot) than is afforded other community centres.

[29] A table in the Respondent's evidence set out details of 28 class "A" and "B" big box 14,000-40,000 square foot stores. For this type of space, a city-wide analysis is made because of the relatively small number of examples available. The table (which was noted "not including enclosed malls") supported the \$17.00 rent rate applied to the subject space.

Board's Decision With Reasons:

[30] The capitalization rate to be applied in the income approach assessment valuation for the subject property is set at 7.75%.

[31] The typical rent rate applied to the subject big box 14,001-40,000 square foot space is reduced to \$14.00 per square foot.

[32] **Capitalization Rate:** The property sales analysis period was argued. The Complainant used sales as old as 29 months and argued that if the Respondent utilizes lease data going back 30 months, then the same period should be used for sales. The Respondent's position is that it is acting consistently on a year over year basis by using just 24 months of sales history but it uses lease data going back 30 months in order to have pertinent data as at the date of

sale. By extending the sales period, the Complainant used two shopping centre sales that were not included in the Respondent's capitalization rate analysis. Other than to point out that these two sales were outside of the Respondent's analysis period, neither of the sales was disputed. It was pointed out that the Respondent uses a longer sales period for other property types such as industrial. The Board finds that there is no set sales analysis period in a capitalization rate study. In any year, there are far fewer sales transactions than there are lease transactions. For this reason, the Board finds that a greater number of sales in an analysis should lead to a better supported conclusion. Accordingly, weight is given to the sales of McKnight Village Mall (5220 Falsbridge Gate NE – Method I Cap. Rate: 8.25%) and to Chinook Station Office Depot (306 Glenmore Trail SW – Method I Cap. Rate: 8.37%).

[33] The Board examined each of the analysis methods put forward by the Complainant. Method I appears to be similar to that used by the Respondent (even though the Respondent denies that it uses that method). Method I used income as set by the Respondent in making assessments of the individual properties. While there are disagreements over the derivation and amount of income to use in each analysis, there is some consistency in the results of the Complainant's Method I and the Respondent's analysis. Method II was found to be less reliable because it appears to incorporate some market rent data along with typical vacancy and other allowances that have been applied by the assessor.

[34] Turning to the sales that were used by the parties, there were five that were common to both analyses. For three of these five, the input factors were the same or highly similar, resulting in capitalization rates that were the same. This finding relates to the Complainant's Method I capitalization rate analysis. The three property sales were: Pacific Place (7.00% cap.), Sunridge Sears (6.55% cap.) and Calgary East Retail (8.85-8.89% cap.). The Respondent insisted that its capitalization rate study is conducted in a different manner than that of the Complainant but the fact is that the incomes and thus the capitalization rates were the same or similar for these three property sales.

[35] The Respondent provided some summary support for the income amounts used in the analysis of each sale. Although limited, it did provide the Board with some background that assisted in forming the decisions regarding acceptable sales. The Board did not receive an acceptable explanation of the final 7.25% capitalization rate that came from an analysis where the median rate was 6.77% and the mean average rate was 6.71%. In an assessment regime where capitalization rates are measured in increments of 0.25%, the selection of a rate as much as 0.54% more than the averages is unacceptable unless there is some rational explanation for that variance.

[36] The Board gives less weight to the rates derived for Cranston Market and Braeside Shopping Centre. The Assessment Business Unit (ABU) changed the rating or classification of these two properties from one year to the next. Each of the parties had analyzed these sales using different criteria because of the differing ratings/classifications. The Board finds that neither of the analyses is supported by market evidence to a sufficient extent. The buyers and sellers of these properties probably paid no heed to the ABU ratings or classifications. These market participants would have based their sell or buy decisions on the actual economics and physical states of the properties. None of that market information was provided so the Board reduced the weight given to these sales. It was not possible to determine whether one party's analysis was more realistic or reliable than that of the other party.

[37] The sale of the Market at Quarry Park shopping centre has been entered into evidence at a number of CARB hearings over the past couple of years. Sometimes, it is accepted as an arms-length, open market sale and sometimes it is not. This Board rejects that sale as being representative of an open market sale. The sale was reported as being inclusive of a 100 room

hotel which was to be built (it has not been built). A daycare centre was also to be added. A nearby office building had been transferred between the same seller and buyer as the shopping centre and it was not clear whether there was a "package price" or whether each property had been priced on its own merits. Several thousand square feet of lease space was headleased by the vendor but no terms of the headlease were in evidence. The Board finds that this transaction cannot be relied upon as an indicator of a market driven capitalization rate.

[38] There was evidence and argument from both parties regarding Assessment to Sales Ratios (ASR's). The Board finds that there is no satisfactory evidence to support the position of either party so neither ASR analysis is given weight in this decision. On the Respondent's side, it was stated that the time adjustment process involved an analysis of all retail property in the city, not just community or neighbourhood shopping centres. Within the universe of properties included in the analysis could be ones where sales occurred more than two years ago. This practice could tend to weight time adjustments to market conditions that were significantly different than they would have been at the time when a particular property sold. It seemed illogical that the application of a time adjustment was firmly tied to dates. For example, two of the property sales that were in the capitalization rate studies sold just four days apart in December 2009. Each of the sales was given a different time adjustment in bringing the historic price to the July 1, 2011 valuation date. The explanation was that sales that occurred after mid-month were not adjusted for that month whereas sales that occurred prior to mid-month were adjusted for that month. One of the sales occurred December 14, 2009 (one day prior to mid-month) and the other occurred December 18th. Four methods of time adjustment measurement were described. The Respondent used three of the methods while the Complainant used one. The Respondent calculated mean and median averages for its three rates (one of which was mathematically incorrect) which were impacted by the one method that the Respondent said was the least reliable. The Complainant based its analysis on an income comparison over time, concluding that the same time adjustment rate would apply to all of its sales in the analysis. These many unexplained and unfounded analysis techniques and outcomes fell short of convincing the Board that an ASR check on sale prices was useful.

[39] From the five sales that the Board finds are most reliable, the median and mean average capitalization rates are 8.25% and 7.81%. These suggest that the 7.75% rate requested by the Complainant is not overly optimistic or pessimistic.

[40] **Rent:** At issue for the derivation of rent rates for the big box 14,001-40,000 square foot space category was the availability of suitable comparables. The Complainant provided data on one enclosed mall lease. That lease was in Westbrook Mall which, like Beddington Towne Centre, is a "B" class property. The Board accepted that lease as the best available comparable. The list of big box leases provided by the Respondent was not given weight by the Board for two reasons: 1. It specifically stated that the survey did not include enclosed malls which implies that malls are treated differently than non-enclosed shopping centres and, 2. The survey included both class "A" and "B" properties and there was no indication of which class each of the properties was in. The Respondent has stated that enclosed malls are treated differently than non-malls and that is shown by the granting of a higher operating cost allowance. Where the Respondent's analysis fails is that rent rates are taken from big box lease samples from non-malls where tenants would be aware of lower operating costs. Most tenants consider their total costs of occupancy and it is logical that those tenants would hold out for a lower rent rate when operating costs are \$21.00 per square foot instead of \$8.00 per square foot. The Complainant's evidence tends to support this concept. The subject ARFI was provided to the City in April 2011. The London Drugs lease data shows a 15 year term from August 13, 1996 which means that the term would have expired in August 2011. Any potential renewals

might not have been known in April when the ARFI return was made. Lease summary data in the Complainant's evidence does indicate a lease start date of August 13, 2011. The Board is satisfied that the subject lease was renewed near the effective valuation date and the specified rent rate was set at \$14.00 per square foot.

[41] The 2012 taxable assessment on this roll number (180077604) is reduced from \$42,520,000 to \$38,810,000. There was discussion between the parties about the handling of the tax exempt space in the recalculation of the assessment. The tax exempt assessment amount of \$1,050,000 is on a different assessment roll number and that roll number is not the subject of a complaint. That assessment amount, however, is calculated on the same basis as the taxable portion. Therefore, if the capitalization rate, for example, is changed for the taxable assessment which is the focus of this complaint, then the tax exempt portion should be recalculated using the same rate. The problem is that the tax exempt roll number is not under complaint so the Board has no authority to change that assessment. In order to put the correct taxable assessment on the roll, the correctly calculated tax exempt assessment must be taken into account. The Board accepted this premise in accepting the revised taxable assessment of \$38,810,000. The Board is aware that the sum of the taxable and non-taxable amounts does not equal the total property valuation however the taxable amount is correct. The non-taxable amount that remains on its own roll number is high but no tax is paid on that assessment amount so no party is being treated unfairly.

DATED AT THE CITY OF CALGARY THIS 27 DAY OF September 2012.



W. Kipp
Presiding Officer

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

NO.	ITEM
1. C1	Complainant Disclosure
2. C2 (Common to several files)	April 13 th 2012 City of Calgary ABU Response to 299/300 Request for Information 2012 Assessment Review Board – Reference Appendix Submission
3. C3 (Common to several files)	Neighbourhood-Community Shopping Centres 2012 Capitalization Rate Analysis & Argument – Appendix
4. C4 (Common to several files)	Neighbourhood-Community Shopping Centres 2012 Capitalization Rate Analysis – Rebuttal Submission
5. 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.*

For Internal Use

Appeal Type	Property Type	Property Sub-Type	Issue	Sub-Issue
CARB	Retail	Neighbourhood Mall	Income Approach	Capitalization Rate Rent Rate