



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:

12-10 Capital Corp. (as represented by MNP LLP), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

PRESIDING OFFICER: T. Helgeson

BOARD MEMBER: J. Kerrison

BOARD MEMBER: Y. Nesry

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 2013 Assessment Roll as follows:

ROLL NUMBER: 067233304

LOCATION ADDRESS: 1216 10th Avenue SW

FILE NUMBER: 70557

ASSESSMENT: \$14,540,000

This complaint was heard on the 9th of July, 2013 at the office of the Assessment Review Board located at Floor Number 3, 1212-31 Avenue NE, Calgary, Alberta, Boardroom 8.

Appeared on behalf of the Complainant:

- *G. Worsley*
- *W. Van Bruggen*

Appeared on behalf of the Respondent:

- *R. Ford*

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

No procedural or jurisdictional matters were raised before the Board.

Property Description:

The subject property is located in the BL4 submarket region of the Beltline, the subject property is comprised of a building with 57,527 square feet ('sq. ft.') of office space on a parcel of land 43,026 sq. ft. in area. The building was constructed in 1974. The building has been classified for assessment purposes as a 'B' class building.

Issues:

1. Is there environmental contamination on the subject property?
2. What is the appropriate vacancy rate for the subject property?
3. What is the appropriate cap rate for the subject property?
4. What is the correct assessed value for the subject property?

Complainant's Requested Values: Option 1: \$12,360,000
Option 2: \$10,600,000

Summary of the Complainant's Submission

[1] The assessment amount is not reflective of the correct application of the assessment range of key factors and variables. These include location, parcel size, improvement size, land use, and influences. The assessment amount is also not reflective of the correct application of either the comparison or income approach, and the Respondent has failed to recognize the negative influences that affect the subject property.

[2] The valuation model does not indicate the correct relationship between the subject property's characteristics as at December 31 of the assessment year, and their value in the real

estate market. The assessment is neither fair nor equitable in relation to similar properties. The negative location indicates the subject property to be similar to a "C" class office.

[3] Specifically, the assessment valuation does not properly consider the location, zoning, building area, physical condition, or parking of the subject property. Sales do not support the Respondent's overall rate per sq. ft. for office.

[4] The rental rate applied to the subject property should be no more than \$13 per sq. ft. There are contamination issues with the subject property, thus a negative 15% influence must be considered. The capitalization rate should be 6.25% (C-1, page 57).

[5] The current assessment does not properly adjust for the negative impact to the subject property's market value due the owner's loss of recoverable expenses. The leases of some tenants have a cap on what they are required to pay in operating costs (C-1, 6th page). Non-recoverables should not be less than 3%. The value attributed to the parking component is unfair and incorrect. In the result, the assessment amount is neither fair nor equitable.

[6] The subject property was previously owned by Canadian Pacific Limited from 1900 to 1972. Since 2006 Golder Associates and Troy Environmental Consulting have completed phase II environmental assessments each year, and determined there are elevated levels of "Perc", a chemical associated with dry cleaning. Although wells were drilled and water pumped until the level of the chemical fell, but there does not seem to be any yearly reduction of the Perc levels, and it appears that efforts to deal with the contamination will be ongoing. The costs of remediation are in the range of \$80,000 per year.

[7] The problem with a contaminated property is that it raises issues of liability. If the subject property were to be sold, the fact the subject property was contaminated would have to be disclosed, and the disclosure would have a negative effect on the sale price. In previous decisions, the Board has considered a 25 – 30% reduction to deal with the issue of contamination. In view of these decisions, the Complainant is justified in seeking a 15% reduction in the assessment value, for clearly there are environmental concerns that must be remediated every year (C-1, page 17).

[8] With respect to rental rates, the Complainant has determined that the Respondent has used only the last three months of the valuation period to derive the office leasing activity for the entire year. When other time frames are considered, the results of this rental rate study vary greatly, and are inconsistent with the time frames analyzed for other sectors. The Complainant has included the complete list of the Respondent's entire rental rates along with the median rates calculated for each time frame, and determined that the median leasing activity is dependent on the time frame considered.

[9] The only periods when the median is \$15 per sq. ft. or more are the two month median, the four month median, and the five month median. All the other time frames indicate that the median rental rate should be between \$14 to \$14.50 per sq. ft. The Respondent used only the last three months of the valuation period to derive the office rental activity for the entire year. Also, the Respondent has considered all of the B class buildings in the Beltline when calculating the lease rate. The Complainant has broken the lease analysis into its respective submarkets and determined the leasing activity in each market (C-1, page 27). Note that 620 12 Avenue SW was left out of the analysis because the building should have been classified as an "A" class office, this because after the fire, over 1.7 million was put into the building to restore it.

[10] The Complainant found that the Respondent used only the last three months of the valuation period to derive the office leasing for the entire year. When other time frames are considered, the results of the rental study vary widely. This year, the only market which has not been split into separate submarkets is the Beltline. The Complainant knows that there are differences between each submarket, hence all leasing activity should not be lumped together (C-1, page 18).

[11] When the Respondent was calculating the vacancy rate for Beltline properties, "AA", "A", "B", and "C" buildings were lumped together. The vacancy rate was not calculated this way for downtown or suburban properties (C-1, page 39). The Complainant has broken out each of the "AA", "A", "B", and "C" class buildings, and has calculated the vacancy for each classification. The average for "B" class is 11.25% (C-1, page 43).

[12] Now to capitalization ("cap") rates. The Respondent's cap study (C-1, page 45) includes the "Cooper Blok" building at 809 10th Avenue SW. This building should not have been included in the study because it was part of a portfolio sale of four buildings, which sold at a total cost of \$142 million. Similarly, the "Keg building" at 605 11th Avenue SW (R-1, page 231) was not brokered, hence not exposed to the market, therefore it too should not have been included.

[13] The Respondent is currently using income parameters from July 1, 2010 to July 1, 2011 to calculate the cap rate for sales that occurred between July 1, 2011 and December 31, 2011. Thus the rents used for calculating the net operating income ("NOI") are offset six months from the sales that are being used to calculate the cap rate.

[14] The correct method is to use the income parameters derived from the period of time when the sales occurred. The Complainant suggests that the income parameters from July 1, 2011 to July 1, 2012 should be used to calculate the cap rate for sales that occurred from July 1, 2011 until July 1, 2012. The Respondent will protest, and argue that sales which occurred from July 1, 2011 to December 31, 2011 have more in common with the rents derived from July 1, 2010 until July 1, 2011 than the rents that have been derived from July 1, 2011 to July 1, 2012 (C-1, page 47).

[15] The Complainant counters the Respondent's argument by noting that because the Respondent uses the median rent from July 1, 2010 to July 1, 2011, there is no guarantee that the median rent calculated will approximate the leasing activity that occurred between July 1, 2011 to December 31, 2011 (C-1, page 47).

[16] By changing the rental rate parameter to \$14 per sq. ft. for buildings in the BL4 zone, and to \$15 per sq. ft. in the BL3 zone, and the vacancy rate to 11% for all "B" class buildings in the Beltline, the cap rate becomes 6%. Using these parameters results in an average and a median ASR of .9569 and 1.0072, respectively, with a coefficient of dispersion of 4.28 (C-1, page 49).

[17] When the *Duff* building at 525–11th Avenue SW and the *Grondin* building at 1451–14th Street SW are added into the analysis, the cap rate changes to 6.25% (C-1, page 53). The average and median ASR become 1.0296 and .09669 respectively, with a coefficient of dispersion of .0697 (C-1, page 54-55).

[18] The Respondent made the mistake of using incorrect vacancy and rental rates. These were derived for the subject property because the Respondent was looking at the Beltline as one homogeneous area. The Complainant provided evidence that the Respondent's method is incorrect. The reason the Beltline was separated into different sub-markets is to account for differences between each sub-market in terms of rent and vacancy.

[19] The Complainant has developed two options for valuation of the subject property. The first option is based on a rent rate of \$15 per sq. ft., a typical office vacancy of 8%, and a cap rate of 5.25%. With those parameters, the valuation is \$14,541,262. Applying a negative influence adjustment of 15% in recognition of the environmental contamination produces a valuation of \$12,360,000. The second valuation option, based on a typical vacancy rate of 11%, a rent rate of 14 per sq. ft., and a cap rate of 6.25%, results in a valuation of \$10,600,000 (C-1, page 58).

Summary of the Respondent's Submission:

[20] The Complainant is requesting that an office rental rate of \$14 per sq. ft. based on leasing by submarket in the Beltline. The Respondent's 2013 'B' class Beltline office rental summary with a breakdown of leases in BL4 with commencement dates from July 1, 2011 to July 1, 2012 show that the resulting weighted average, \$14.92 per sq. ft., amply supports the assessed rental rate of \$15 per sq. ft. (R-1, page 25). Municipal Government Board Order 045-09 directs the use of weighted averages to determine typical rates.

[21] The Complainant has combined all Beltline office classes and performed an analysis to determine that the overall typical office vacancy rate is 11%. The Respondent has reviewed the Complainant's 'B' class office study, and made some needed changes. The corresponding study with corrections is provided (R-1, pages 26–28), and indicates an office vacancy of 7.44%. With the corrections, the Complainant's vacancy analysis comes in with a typical rental rate of less than 8%.

[22] The Complainant is requesting a cap rate of 6.25%. In doing so the Complainant deleted two sales relied on by the Respondent, and then added two sales. The Complainant has also relied on a different time frame than the Respondent's when determining the income parameters for the cap sales. The Complainant's ASR studies for the cap sales have been done incorrectly.

[23] The Respondent will speak to the sales the Complainant included in its cap rate study, sales that were excluded by the Respondent. The Complainant used different income parameters in regard to the Grondin building at 1451 14th Street SW, and used it in both their office and retail cap studies. The Grondin building should be considered a retail building, not an office building.

[24] The other building used in the Complainant's cap rate study is the Duff building at 525 11th Avenue SW. The Duff building was purchased in 2011 for its development potential, and sold in 2013 for more than twice its 2011 purchase price.

[25] With respect Phase II environmental report included in the Complainant's material indicates that the subject property has contamination issues. The Respondent will provide the most recent report available from the Environmental Site Assessment Repository (ESAR) with respect to the remediation of groundwater at 1201-1238 10th Avenue SW. The IAAO standards

on contamination and valuation of these properties, also their affect on market value. The sale documents relating to the subject property will be reviewed, along with a non-residential sales ARFI indicating that the purchasers do not believe there are any features that affect the property in a negative way, i.e., environmental concerns.

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

[26] During the hearing, the Complainant emphasized the fact that the Respondent has rolled the nine submarket areas in the Beltline into one, making the Beltline a single homogeneous market. The Complainant spent a great deal of time and effort to demonstrate to the Board that it was this new homogeneity that caused the assessor's typical rental rate for the subject property to be at \$15 per sq. ft. instead of \$14 per sq. ft.

[27] Nevertheless, the Respondent brought the BL4 submarket back to life once more, and developed a B Class rental rate summary with leases that commenced from July 1st, 2011 to July 1st, 2012. The result is a weighted average of \$14.92 per sq. ft. (R-1, page 21). This settles the issue of the correct rental rate as far as this Board is concerned, just as it did in the decision for File #70519.

[28] As for typical vacancy, that matter as well was settled in the decision for File #70519, for was agreed between the parties that applicable evidence and argument from the hearing for the 'lead' file, #70519, would be carried forward. The Board understood "carrying forward" to mean findings and matters decided in file #70519 might also be carried forward in cases where the issues and facts are the same or very similar. If the findings and decisions in the lead case were ignored, the result would be inconsistency throughout. The vacancy rate will remain at 8.00%.

[29] With respect to the matter of the appropriate capitalization rate ('cap rate'), the Board notes that the Complainant has relied on one of the same cap rate studies it used in the hearing for File #70519. That study can be found at page 53 of C-1 in this matter. It was not clear at the time and it remains unclear why three properties in the study are shown with a rental rate of \$14.00 per sq. ft., and the two remaining properties are shown with a rental rate of \$15.00 per sq. ft. This study appears to be mixing and matching properties of different classes.

[30] There is another cap rate study, this one at page 246 of C-4, the Rebuttal in this matter. It is the very same cap rate study that appeared in C-4 of File #70519. This cap rate study shows four of the properties that appear at page 53 of C-1, all with rental rates of \$15.00 per sq. ft., under the heading 'MNP's Capitalization Rate Study– Beltline 7 months to July 2012'. The Board found that, for the most part, the NO's in this study were from 2013 assessments.

[31] One of the properties at page 239 of C-4 in File #70519, 1410 1 Street SW, was excluded by the Board because it was new evidence. That same property is in the study at page 246 of C-4 in the matter at hand, and by parity of reasoning, it is also excluded from the present matter. Three of the properties, 1520 4th Street SW, 906 12th Avenue SE, and 1207 11th Avenue SW, are also included in the Respondent's cap rate study. After argument from the parties during the hearing on File #70519, the Board accepted these three properties as suitable candidates for a cap rate study, and the result was a cap rate of 6.15%. Upon hearing the same arguments yet again, the Board finds no reason why the cap rate of 6.15% should not stand, and apply in the case at hand.

[32] The Board finds that the Respondent failed to recognize a negative influence that affects the subject property. The negative influence is environmental contamination. Although none of the addresses of the affected properties mentioned in the 2006 Phase II Environmental Site Assessment (C-1, pages 110 & 111) match the address of the subject property, the Board is able to determine through juxtaposing pages 110 and 111 with the air photographs on pages 14 and 19 of R-1, that the subject property is in fact that the property shown as 1210 10th Avenue SW on pages 110 and 111 of C-1.

[33] In the Executive Summary of the Phase II Environmental Site Assessment, the Board finds these words (C-1, page 72):

"Based on laboratory analysis of confirmatory soil samples collected during the investigation, tetrachloroethylene, a volatile organic compound, was reported at a concentration in excess of the applicable site criteria in a soil sample collected from borehole MW3."

"The calculated dissolved solids (TDS) value in the groundwater samples collected from MW1, MW2, MW4, MW5 and the replicate sample (MWO6-08) exceeded the applicable regulatory criteria."

The Board finds nothing in the 2008 Groundwater Remediation Program (R-1, pages 47 to 185), to dissuade it from a finding that the subject property is contaminated.

[34] Turning to the *Standard on the Valuation of Properties Affected by Environmental Contamination*, a publication of the International Association of Assessing Officers, copyrighted 2001, the Board finds these relevant comments (R-1, pages 182–203):

3.3 "In evaluating the effect these conditions on market value, consideration should be given to public perception and fear, which may affect values in the marketplace."

3.3.1.1 "Even after cleanup is completed, owners may be liable for additional cleanup of contamination not discovered initially. Often costs exceed initial estimates and affect market-ability of property and income streams for a long time."

The Board finds that the absence of mention of an environmental problem in either the sale documents for the subject property or an ARFI is not conclusive evidence that there is no contamination on the subject property (R-1, pages 206 – 212). The subject property is contaminated, and should have an influence adjustment of minus 15%.

The Board's Decision:

[35] A cap rate of 6.15% and an influence adjustment of 15% results in an adjusted assessment of \$10,500,000, as rounded. It is so ordered.

DATED AT THE CITY OF CALGARY THIS 29th DAY OF November 2013.



Presiding Officer

Exhibits**C-1, Complainant's Evidence Submission****C-2, Disclosure, evidence****C-3, Disclosure, evidence****C-4 Rebuttal****R-1, Respondent's Assessment Brief**

<u>Appeal Type</u>	<u>Property Type</u>	<u>Property Sub-Type</u>	<u>Issue</u>	<u>Sub-Issue</u>
CARB	Office	Low Rise	Income Approach	Cap rate

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.*