



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:

Community Natural Foods Ltd. (as represented by MNP LLP), COMPLAINANT

and

The City Of Calgary, RESPONDENT

before:

T. Helgeson, PRESIDING OFFICER

Y. Nesry, BOARD MEMBER

J. Kerrison, BOARD MEMBER

This is a complaint to the Calgary Assessment Review Board in respect of a property assessment prepared by the Assessor of The City of Calgary and entered in the 2013 Assessment Roll as follows:

ROLL NUMBER: 067233908

LOCATION ADDRESS: 1003 11 Street SW

FILE NUMBER: 70594

ASSESSMENT: \$6,900,000

This complaint was heard on the 12th day 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:

- *W. Van Bruggen*

Appeared on behalf of the Respondent:

- *D. Zhao*

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 a parcel of land comprising 29,871 square feet ("sq. ft."), situated in the BL4 submarket of Calgary's "Beltline". Located on the parcel of land is a building that was constructed in 1978. The area of the building is 22,460 sq. ft.

The Respondent has classified the building as a "B+" class building, but the subject property has been assessed as land only. The assessor has applied a negative adjustment of 15 percent due to proximity of the subject property to the railway tracks.

Issue:

1. Is the assessment based on highest and best use of the subject property as vacant land?
2. Has the Respondent assessed the subject property in accordance with the *Act* and associated regulations?
3. If the assessment is not in accordance with the *Act* and associated regulations, what is the correct assessment?

Complainant's Requested Value:

Either \$5,890,000 based on the income approach to value, or \$6,272,000 based on a land based sales approach.

Summary of the Complainant's Position

[1] The assessment amount is incorrect because it does not comply with the *Municipal Government Act* ("the *Act*") or the requirements of AR 220/2004, the *Matters Relating to*

Assessment and Taxation Regulation ("MRAT"). Section 289(2)(a) of the *Act* requires that each assessment *must* reflect:

- (a) *the characteristics and physical condition of the property on December 31 of the year prior to the year in which a tax is imposed under Part 10 in respect of the property, and*
- (b) *the valuation and other standards set out in the regulations for that property.*

The physical characteristics of the subject property at December 31 of the assessment year are not reflected in the assessment. This is so because the subject property has been assessed as vacant land. As of December 31 of the valuation year, the subject property was occupied as an office building, there were no development permits or applications for development permits that would indicate a change in use was forthcoming or even contemplated.

[2] Section 293(1) of the *Act* stipulates that in preparing an assessment,

"... the assessor must, in a fair and equitable manner,

- (a) apply the valuation and other standards set out in the regulations, and*
- (b) follow the procedures set out in the regulations."*

If there are no procedures in the regulations for preparing assessments, s. 293(2) provides that, *"... the assessor must take into consideration assessments of similar property in the same municipality in which the property being assessed is located."*

[3] Nor does the assessment reflect the correct application of the range of key factors and variables relied on in assessing property, e.g., location, parcel size, improvement size, land use, and influences. Furthermore, the assessment does not reflect a correct application of the comparison or income approach as a primary or secondary approach to value.

[4] The assessment is neither fair nor equitable relative to similar properties in Calgary. In particular, the assessment does not properly consider the location, zoning, building area, physical condition, or parking of the subject property. The assessment does not adequately account for atypical deficiencies in the subject property as of the characteristics and condition date, December 31st of the year prior to the tax year. Further, the Respondent's sale comparables are not a comprehensive list of properties that sold between July 1st, 2010 and the valuation date of July 1st, 2012.

[5] The assessment was incorrectly calculated based on an unfounded assumption that the highest and best use for the subject property is as land for redevelopment. This error has resulted in an assessment in excess of market value, also an assessment that is inequitable compared to comparable properties.

[6] There is no reasonable probability that redevelopment of the subject property is financially feasible, physically possible or legally permissible as at December 31 of the assessment year. The Respondent has determined that the highest and best use for properties is as bare land. The criteria the Respondent relies upon is whether the value of the building derived using the income approach is greater than the value of land only. The result of this error

is an assessment for the subject property that is neither fair nor equitable.

[7] The first problem with the Respondent's method of determining the highest and best use for an improved property is that it does not consider the demolition cost for the subject property. Without the original improvement being removed, it would be impossible to redevelop the site. *The Appraisal of Real Estate – Third Canadian Edition*, states:

"In practice, a property owner who is redeveloping a parcel of land may remove an improvement even when the value of the property as improved exceeds the value of the vacant land. The costs of demolition and any remaining improvement value are taken into consideration in the test of financial feasibility for redevelopment of the land."

[8] In the case of the subject property, the remaining improvement value would be would be significant because the entire building has been leased out. To develop the subject property the owner would have to bear some steep legal costs for breaking the leases. Since the building has 22,460 sq. ft. of office space and 52 parking stalls, using the Complainant's derived income parameters and a lease term of five years, the current value of the income stream for the subject property would be \$1,584,390 (C-1, page 5).

[9] The subject property was constructed using reinforced concrete. The *Marshall and Swift* demolition costs estimator indicates that demolition costs will be in the range of \$3.79 to \$4.95 per sq. ft. with a local multiplier of 22% to 36%. Being conservative, the Complainant has used the low end of both ranges, and determined that the demolition cost per sq. ft. would be roughly \$4.62 per sq. ft. As the area of the subject property is 22,460 per sq. ft., this would result in a cost of \$100,000, a significant cost to be considered.

[10] Therefore, the total cost of removing the improvement would be $\$1,541,700 + \$100,000 = \$1,641,700$. When this cost is subtracted from the current assessed value of the land, i.e., $\$220 \times 29,871 = \$6,900,000$, the result is \$5,258,300, a value significantly less than the value derived using the income approach (C-1, page 6).

[11] *The Appraisal of Real Estate – Third Edition* also states that when doing a highest and best analysis on a parcel of land, there are four tests that must be considered, i.e., whether the highest and best use is (1) legally possible, (2) physically possible, (3) financially possible, and (4) maximally productive (C-1, page 6). The Respondent considers the first two tests by using the value of land that is zoned the same as the subject property, but when it comes to the last two tests, the Respondent ignores them.

[12] In regard to the third test, *The Appraisal of Real Estate – Third Edition* states: "The level of analysis may vary with assignments, but the economic demand for the subject is a prerequisite to the financial testing of all alternatives". There are 3,913,860 sq. ft. of "B" class office space in the Beltline, and of this space 440,129 sq. ft. is vacant, amounting to a vacancy rate of 11.25% (C-1, pages 25 – 26).

[13] Further, according to the CRESA market report, the absorption for both downtown and Beltline properties is as follows: Q1 2012: -5,669 sq. ft., Q2 2012: 109,560 sq. ft., Q3 2012: -85,486 sq. ft., and Q1 2013: -90,120 sq. ft. Given the amount of office space available, and the current trend for "B" class office space, it does not seem likely there would be sufficient demand for additional office space beyond what is currently under development.

[14] The second consideration is the amount of vacant land for development. The Complainant was able to identify sixty parcels of land between the CPR tracks and 17th Avenue, accounting for more than 1,000,000 sq. ft. of space appropriate for development (C-1, pages 8-9). This survey omits parcels of land with improvements that the Respondent has valued as land only; if all these parcels were considered it would double currently available land. With this amount of land available, it is unlikely that an owner would be willing to give up a fully occupied building to redevelop the land.

[15] Equity is another factor that the Respondent failed to recognize in valuing the subject property as vacant land. Six "B" class properties, all with floor area ratios (FARs) less than one, were valued using the income approach. One of these six properties, 1313 10th Avenue SW, was valued as land last year, but oddly, this year the property was valued on the income approach (C-1, page 11). The Complainant is asking only that the subject property be fairly assessed in comparison to other "B" class Beltline properties, and for this reason the subject property should be valued based on the income approach.

[16] MNP has conducted a land analysis (C-1, page 28), and determined that the value of land in BL3, BL4, BL6, BL7 and FS1 of the Beltline should not be valued any higher than \$200 per sq. ft. Three of the six sales in the analysis had significant improvements on them at the time of sale. Because these properties have improvements of some kind, it was necessary to strip off the improvement value for each property.

[17] The Complainant requests that the Board consider the evidence before them in defence of the subject property being valued on the income basis. The Complainant has determined that when the demolition costs of the improvement and the cost to break the lease are considered it would reduce the property to below the value of the property if it were assessed on the income approach.

[18] The Board in previous decisions has determined that the subject property should be valued based on its physical characteristics as at December 31 of the assessment year. At that date in 2012, the subject property was an office building. Further, there is no indication that the Complainant has any intention of redeveloping the site. No development permits have been applied for, and currently the building is fully leased. Unless the subject property is to be redeveloped in the near future, the highest and best use is the present use and condition of the subject property.

Summary of the Respondent's Position

[19] The issue before the Board is this: what is the market value of the subject property? The Complainant asserts that the subject property should be valued by the income approach, and has provided information to support its argument. The Complainant has also included a land value analysis.

[20] The purpose of property assessments is not to reflect one sale price, but to assess all similar property at a similar value so that taxation is fairly and uniformly distributed among taxable property. The Respondent *must* assess properties at market value. Market value can be determined using any of the three approaches to value, i.e., the sales comparison approach, the income approach, and the cost approach. The Respondent is not legislated to apply one

approach to value in arriving at market value. Where the land value estimate exceeds the capitalized income value estimate, the Composite Assessment Review Board has established that the property's land value best represents its market value.

[21] The land use of the subject property is CC-X with an FAR of 5.0. This indicates that the maximum building size of an improvement can be much larger than the actual building area. The Respondent will provide the land sales and supporting information relied on to derive the rate of \$220 per sq. ft. (R-1, pages 27 – 82) used to arrive at market value for vacant parcels as well as improved properties in the Beltline where the income approach does not reach land value, as in the case before the Board.

[22] The Respondent will demonstrate that 1002 14 Street SW was a court ordered sale, and is located in BL5, not part of the group the Complainant was analyzing, hence should not be included. Further, the Respondent will show that the Complainant used 1451 14 Street SW in two different capitalization studies, and have used different income parameters.

[23] In response to the Complainant's notion that an income producing property must be valued using the income approach, there is the example of an improved property in the Beltline that sold for more than its assessed value (at p. 6 of R-1). When the Direct Sales approach was applied using the vacant land rate, the assessment became much more reflective of market value, thus proving that purchasers have paid more for properties than their income generating potential would indicate.

[24] Due to this and other reasons to yet be explained, Beltline income parameters at the valuation date have exhibited an effect whereby the improvements to the subject property were exposed to a market-driven influence that resulted in an inability to produce a capitalized income value that exceeds the established land value in the area. More importantly, this has resulted in a capitalized income value that is incapable of reflecting market value. Clearly, the improvement on the subject property is not the value-driver, thus the income from it cannot be capitalized to represent market value.

[25] The City of Calgary must assess properties at market value. In cases where an estimate of land value exceeds the capitalized income value, the Composite Assessment Review Board ("CARB") has established that the land value of the property best represents market value. In Board decision ARB 1191/2010-P, the Board had this to say at paragraph 6:

"The Assessor went on to say that the value derived through application of the Income Approach as applied by the Complainant was less than the bare land value estimated for the subject property and that is precisely why the land value has been applied. The reasoning of the assessor is clear to the CARB and it is based upon well founded valuation theory. If the improvements to a given property are of such an age or design or other influence that results in the property being incapable of producing a capitalized income value that exceeds the established land value, then the land value represents the market value of the property."

[26] The logical notion is that any willing seller would hesitate to sell their property for less than its land value. Neighbouring properties have been valued in the same manner as the subject property when their income values are less than their established land value. This creates and maintains equity.

[27] The land use designation of the subject property under the Land use Bylaw is CC-X, with an FAR of 5.0. The maximum buildable area of a new improvement is much greater than the building area of the existing improvement. It is reasonable to suggest that the income approach cannot represent market value for the subject property. Instead, the most reasonable representation of market value is the land value of the parcel. It is inequitable to have improved parcels assessed for less than unimproved parcels of comparable form.

[28] Applying land value to both improved and unimproved parcels would establish equity, supporting the Respondent's implementation of land only as the lower threshold for assessment value. Point 9 in ARB 0105/2007-P supports this concept:

9) The Board accepts that there are instances where the "highest and best use" principle is appropriate. These instances occur where the market value for the land only establishes a threshold for value, that is, a value established by the market in which values above the threshold will occur, but values below will not. (R-1, page 10)

To lower the assessment of the subject property to the complainant's requested value would create inequity with other commercial properties in the Beltline, both improved and unimproved, and would also set the assessment well below market value as of July 1, 2012.

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

[29] The Board finds that the assessment of the subject property does not reflect the characteristics and physical condition of the subject property as at December 31 of the year prior to the year in which a tax is imposed, as required by s. 289(2) of the *Act*. This finding leads to another issue, i.e., what is the result of preparing an assessment that fails to recognize the characteristics and physical condition of the subject property as of December 31, 2012? There is no provision in the *Act* that would render the assessment of the subject property null and void, nor is there a penalty provision. In the absence of a ruling of the Court of Queen's Bench, the only test that applies is market value. If the assessment does not reflect market value, it must be corrected.

[30] The Board finds that the Respondent is not basing the assessment of the subject property on highest and best use, although one might get that impression by the Respondent's use of words, i.e., *"The land use of the subject property is CC-X with an FAR of 5.0. This indicates that the maximum building improvement size is much greater than the actual building area . . ."* (R-1, page 8). It is the Land Use Bylaw that designates the subject property as CC-X with an FAR of 5.0, the actual use is something else entirely.

[31] What the Respondent does is assess the land of the subject property by the sales approach. The Complainant states that the Respondent relies on values of land zoned the same as the subject property (C-1, page 6). The Respondent submits that the sales approach produces an assessment that reflects market value, as defined in s. 1(1)(n) of the *Act*. The Respondent's rationale is that the land value of the subject property supersedes any value attributable to the office building on the subject property. As stated by the Respondent, the office building is not the "value-driver". The Board agrees that in this matter, the income approach to value would likely result in a value considerably below market value.

[32] The Complainant asserts that the method used by the Respondent to determine highest and best use for the subject property does not consider all necessary components, and in particular, the fact that the building on the subject property is fully leased. Redeveloping the subject property would require the demolition of the building, and this would end the income stream.

[33] The Complainant says that the improvement value would be significant, since the entire building has been leased out. With 22,460 sq. ft. of office space plus 52 parking stalls, and relying on the Complainant's derived income parameters plus the lease time of five years, the value of the income stream would be \$1,584,390. This income stream, combined with a Marshall and Swift estimation of the cost of demolition, would be \$1,641,700. Subtracting this amount from the assessed value results in an assessment of \$5,258,300.

[34] The Board has serious problems with the Complainant's demolition-based value. First, why would a prospective purchaser rely on the Complainant's derived income parameters rather than the actual rent? Second, there is no evidence of the lease itself, thus the term of the lease, the rent, and the presence of a termination clause are not known. The Board cannot reach a decision where there is insufficient evidence. Further, in regard to the cost of demolition, there is not so much as a pro forma to show how the Marshall & Swift demolition costs estimator worked, nor is there a quote from a contractor.

[35] The Complainant's evidence is that there is almost four million square feet of "B" class office space available in the Beltline, and of this space 440,129 sq. ft. is vacant, and further, that there is 1,039,662 sq. ft. of vacant land (C-1, page 6). The Complainant asserts that with so much land available, it is unlikely that the owner of the subject property would give up a fully occupied building to redevelop the land. Well, that may be, but what would the owner do if someone offered to buy the subject property at a hefty price? The undeniable fact is that purchasers are paying a lot of money for land in the Beltline.

[36] As for equity, the Complainant relies on six properties with a floor area ratio ("FAR") less than one (C-1, page 11). The Complainant avers that these six properties were valued using the income approach. That is all the information there is with respect to these properties. The only thing they have in common with the subject property is a low FAR. The Board finds there is insufficient evidence to determine whether the six properties are comparable to the subject property.

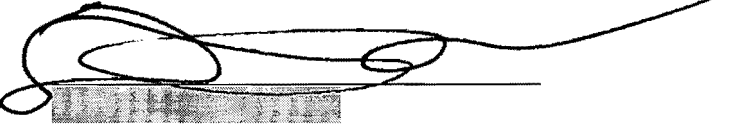
[37] With respect to the Complainant's own sales approach, the land rate analysis at page 28 of C-1 is the same that appeared in file #70592. Three of the six properties in the analysis are subject to "improvement adjustments", being amounts "stripped off" the properties. These improvement adjustments purport to represent the depreciated values of buildings on the properties, and the purpose of deducting the improvement adjustments is to arrive at land values for each of the three properties. The other three properties are vacant in actuality.

[38] The problem the Board has with the improvement adjustments is that there is no information with respect to the arithmetic methodology applied to achieve the depreciated values. In other words, the Board does not know how it was done, and without that knowledge, the Board cannot rely on the improvement adjustments, nor the resulting land values.

Board's Decision:

The assessment of the subject property is confirmed.

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



Presiding Officer

Exhibits

C-1, Complainant's Disclosure Package.

C-2, Complainant's Second Disclosure Package

C-3, Complainant's Rebuttal Package

R-1, Respondent's Assessment Brief

For Administrative Use:

<u>Appeal Type</u>	<u>Property Type</u>	<u>Property Sub-Type</u>	<u>Issue</u>	<u>Sub-Issue</u>
CARB	Office	Stand Alone	Land Sales	Property Value

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.*