

Decision: #0262-466/2012

Complaint ID: 466

Roll: 1633735

---

COMPOSITE ASSESSMENT REVIEW BOARD DECISION

HEARING DATE: SEPTEMBER 27, 2012

PRESIDING OFFICER: M. CHILIBECK

BOARD MEMBER: A. GAMBLE

BOARD MEMBER: V. HIGHAM

BOARD CLERK: S. PARSONS

---

BETWEEN:

First Red Deer Place  
Represented by: Canadian Valuation Group Limited

Complainant

- and -

The City of Red Deer

Respondent

[1] This decision pertains to a complaint filed by First Red Deer Place to the Central Alberta Regional Assessment Review Board (hereinafter, the "RARB"), in respect of a property assessment prepared by the City of Red Deer (hereinafter, the "City"), and entered in the 2012 Assessment Roll as follows:

Roll Number:	1633735
Municipal Address:	4911 – 51 Street, Red Deer, Alberta
Assessment:	16,978,300

[2] The Assessment complaint, including filing fees, was received on March 15, 2012. Disclosure evidence was filed by both parties in a timely manner: the Complainant's initial disclosure on August 14, 2012, the Respondent's disclosure on September 12, 2012, and the Complainant's rebuttal on September 19, 2012.

[3] This complaint was heard by a Composite Assessment Review Board (hereinafter, the "Board"), on September 27, 2012, in City Hall Council Chambers in the City of Red Deer.



[4] Appeared on behalf of the Complainant:

- T. Janzen, Representative of Canadian Valuation Group Limited, Edmonton
- M. Keyes, Lawyer with Warren Sinclair, Red Deer
- R. Martin, Property Shop Manager

[5] Appeared on behalf of the Respondent:

- R. Kotchon, Property Assessor for the City of Red Deer

### **JURISDICTION**

[6] The Board was established in accordance with section 456 of the *Municipal Government Act R.S.A. 2000, ch M-26* (hereinafter, "the MGA") and the *City of Red Deer Assessment Review Board Bylaw 3441/2009*.

[7] Neither party raised an objection to any Board member hearing the complaint.

[8] No procedural or jurisdictional matters were raised by either party.

### **BACKGROUND**

[9] The subject property is a multi-story building comprising 67,487 sq.ft. of office space and 18,653 sq.ft. of main floor retail space (for a total area of 86,140 sq.ft.) – with 51 underground and 57 surface parking stalls, six of which are reserved for visitor parking. The property is commonly known as First Red Deer Place and is located in downtown Red Deer.

### **PRELIMINARY MATTER**

[10] The following Preliminary Matter was brought before the Board:

[11] The Complainant requested that the official record of the hearing be sealed in its entirety. Upon questioning, the Complainant requested in the alternative, that the following specific excerpts from the official record be sealed:

- C1 – Tabs 1 and 6
- R1 – Pages 5, 16, 21, 23, 24-26, 28 and 29
- C2 – All
- R2 – All

[12] The Complainant argued that the excerpts noted above contain sensitive and confidential information pertaining to the business and financial records of its operation, which if disclosed in the public record may adversely affect the Complainant's ability to conduct its operations.

[13] When asked for comments respecting the matter, the Respondent indicated that they supported the Complainant's alternative request for limited sealing of the identified excerpts, and the hearing was then recessed while the Board deliberated the matter.



[14] After re-convening the meeting, the Board rendered the following decision on the preliminary issue: to grant the Complainant's alternate request to have the following excerpts of the official record sealed:

- C1 – Tabs 2 and 6
- R1 – Pages 5, 16, 21, 23, 24-26, 28 and 29
- C2 – Last three pages (Rent Roll, "September-11")
- R2 – Page 2

[15] In support of this decision, the Board relied upon RARB Policy 009/G, which states as follows at paragraph 2 on page 3:

"At the request of a Party, the Board may determine that evidence, or parts of evidence, will be sealed and not available to the public. When considering such a request the Board will consider:

1. whether or not the evidence would be releasable under the provisions of FOIP; and
2. whether the benefits of sealing the record outweigh the benefit of it remaining accessible to the public."

[16] The Board also reviewed and was persuaded by an excerpt from a Municipal Government Board (hereinafter, the "MGB") Decision, Order #034/12, which reads as follows:

"Having reviewed the documents, the MGB accepts their unfettered release may have negative consequences for the Complainants. Accordingly, the documents listed ... are ordered sealed pursuant to Procedure Guide Section 9.3."

[17] Therefore, the excerpts identified in paragraph 12 herein, constituting part of the official record of this hearing, shall be sealed.

## **ISSUES AND FINDINGS**

[18] The Complainant identified one matter on the Assessment Review Board Complaint Form, and attached several paragraphs denoting reasons for the complaint. At the hearing, the Complainant advised that the matter of an assessment amount is under complaint, and identified the following issues for the Board's review, contending that:

1. A main floor office area (comprising 1,080 sq.ft of space) was assessed using a rental rate of \$18/sq.ft., which should be reduced to \$16/sq.ft.;
2. The vacancy allowance rate of 3% applied to the subject property should be increased to 10%; and
3. The Capitalization Rate (hereinafter, the "Cap Rate") of 8.25% applied to the subject property should be increased to 9.25%.

## **COMPLAINANT'S REQUESTED VALUE**

[19] As per disclosure of evidence: \$13,430,000.



## **1. Rental Rate for Disputed Main Floor Area**

### **Complainant**

[20] The Complainant noted that the Respondent assessed the subject property as a high-rise office building, applying lease rates of \$18/sq.ft. to main floor retail areas, and \$16/sq.ft. to office space components of the building – excepting 1,080 sq.ft. of office space on the main floor assessed at \$18/sq.ft., which the Complainant maintains should be assessed at the office rate of \$16/sq.ft. to be fair and equitable.

### **Respondent**

[21] At page 15 of their submissions, the Respondent noted that there are in fact two tenants who occupy the disputed 1,080 sq.ft. main floor parcel: an office tenant, with 630 sq.ft. of space and a retail tenant, with 450 sq.ft. of space.

[22] The Respondent further argued that the City applied a consistent lease rate of \$18/sq.ft. to all main floor office high-rise buildings throughout the city: "This rate reflects the current typical market rate as of July 1, 2011, and is a consistent approach followed in all downtown office buildings." (R.1.-p.15).

### **Board Findings**

[23] The Board concludes that the Complainant lacked persuasive evidence to justify a departure from the Respondent's consistent approach of applying rental rates of \$18/sq.ft. to all main floor space in this category of office buildings.

[24] Of the disputed 1,080 sq.ft. of main floor space, 450 sq.ft of it is occupied by a retail tenant, justifying the typical \$18/sq.ft. rate (actual rent paid by the tenant is \$18/sq.ft., R.1.-p.21).

[25] The fact that the remaining 630 sq.ft of the disputed main floor space is leased to an office tenant with an actual rent of \$14/sq.ft. is a business decision made by the property owner/managers, and entirely within their control to change or maintain.

[26] The Board accepts the Respondent's determination that main floor space is inherently more valuable than upper floor space, given that the Respondent consistently applied the higher \$18/sq.ft. rental rate to all main floor spaces throughout the city for buildings in this category, including the subject property.

[27] Thus, the Board finds the \$18/sq.ft. rental rate applied to the subject property in this case to be fair and equitable.

## **2. Vacancy Allowance**

### **Complainant**

[28] The Complainant noted that the Respondent applied a vacancy allowance of 3% to the subject property, which represented the Respondent's standard allowance for office buildings in this category. The Complainant further noted that a major tenant vacated a large space in the



subject property in August, 2011, and the Complainant identified significant renovation costs associated with preparing that space to be leased out to a new tenant.

[29] Thus, the Complainant maintained that the actual vacancy in the subject property was at 22.7% as of December 31, 2011, comprising 19,504 sq.ft. of space.

[30] The Complainant also noted that a large, new office building with 112,000 sq.ft of space was built in 2010 adjacent to the subject property, and has been on the market for about two years now, with approximately 60,000 sq.ft of available space (54% unleased) as of August, 2012.

[31] The Complainant further argued that "considering the size of the subject property's vacant space, the owners/managers anticipate a considerable time to attract new tenants. Based on the above, it appears that a 10% vacancy allowance could reasonably be applied to the subject property to reflect its condition as of December 21, 2011." (C.1.-p. 2).

### **Respondent**

[32] The Respondent argued that to increase a vacancy allowance from the "typical" 3% applied across the board to this category of properties, the Complainant would need to provide evidence of "chronic vacancy," which the Respondent maintained is not defined in the MGA.

[33] The Respondent further argued that the City maintains a policy with respect to recognizing chronic or extraordinary vacancy, which "is to consider the issue after three consecutive years of vacancy in the same space, [applied] to any non-residential building whether it is commercial, industrial, or office space." (R.1.-p.15 ).

[34] The Respondent also argued that an "annualized vacancy allowance for an individual property is developed through a multi-year (3-5 year) analysis ... and is not a reflection of income loss due to vacant space as of the date of valuation (a snapshot in time)." (R.1.-p.15).

[35] The Respondent noted that tenant rolls provided to the City for the years 2010 and 2011 indicated only one vacant space comprised of 1,982 sq.ft in the subject property during those years, which translates to an actual vacancy of 2.30% for both years, and formed part of the data the Respondent incorporated in its aggregate analysis of vacancy allowance.

[36] The Respondent also contended that the adjacent office building with 112,000 sq.ft of space is not an acceptable comparable – since it is new and condominiumized, it falls within a different assessment category altogether.

[37] Finally, the Respondent concluded that since the subject property "had no long term or unusually large vacancy, applying the typical market vacancy of 3% to the subject property is fair and equitable." (R.1. - p.17).

### **Board Findings**

[38] The Board finds that the Complainant provided insufficient evidence to support its request for a 10% vacancy allowance, and believes the Complainant's request for a 10% rate appears



relatively subjective, since it is not supported by accompanying market data to indicate how the Complainant arrived at that particular number or why it should be accepted by the Board.

[39] The Board was not persuaded by the Complainant's argument relative to actual vacancy experienced by the subject property between August 2011 and the end of December 2011. Tenants come and go throughout the course of any given business year. Non-residential properties are generally assessed with a "typical vacancy" calculation (in this case 3%) to account for ongoing changes inherent in the commercial tenancy environment.

[40] In the absence of persuasive evidence from the Complainant that the typical vacancy rate utilized by the Respondent (3%) is not reflective of market conditions for the applicable period, or evidence that the subject property is plagued by site-specific chronic conditions, the Board concludes that a broader, longer term view of vacancy would be more appropriately applied to the case at hand, and would in fact be more consistent with actual market conditions over time.

[41] Thus, the Board accepts as reasonable the Respondent's position with respect to recognizing chronic or extraordinary vacancy, which is to consider the issue after three consecutive years of vacancy in the same space.

[42] While the vacancy identified by the Complainant (between August 2011 and the end of December 2011) is certainly substantial (22.7%), the Board is not persuaded that it is either long-term or chronic, given the relatively short time span considered.

[43] Thus, the Board finds the 3% typical vacancy rate applied to the subject property in this case to be fair and equitable.

### **3. Cap Rate**

#### **Complainant**

[44] With respect to calculating cap rate, the Complainant argued that the only recent office building sale in Red Deer to compare the subject property to is a building located at 4817 – 48 Street with the following characteristics:

- Two story office building;
- Same age as the subject property;
- Houses the City as sole tenant in the building;
- Gross annual income \$230,025 divided by total square footage 14,500 sq.ft. results in a calculated income rate of \$15.86/sq.ft. (which the Complainant notes is similar to the rental rates used for the subject building);
- Sold in July 2009, with a cap rate of 9.27%

[45] The Complainant asserted that "based on an analysis and comparison of the foregoing sale information to the subject property, and considering all factors affecting its income-producing potential, a capitalization rate of 9.25% is considered appropriate." (C.1.-p.2).

[46] Applying the 9.25% cap rate to its "reconstructed net operating income" and adding their requested 10% vacancy rate, the Complainant produced a "base year market value of \$13,429,900" for the subject property. (C.1.-p.3).



[47] The Complainant then advanced a number of capitalized income calculations, based on a comparison to one other office building downtown, the Professional Buildings, whose cap rate fell by 0.25% from 2011 to 2012 (cap rate for the subject property fell by 0.50% for the same period, which the Complainant maintained was inequitably applied).

[48] Taking the data used to assess the Professional Building (\$14/sq.ft. lease rate, 3% vacancy rate, and 8.5% cap rate), the Complainant calculated a property value of \$182.19/sq.ft. for the Professional Building (including its parking structure assessment).

[49] Based on a 10% vacancy rate (Complainant's requested rate) and a 9.25% cap rate (based on the lone sale comparable), the Complainant produced a "combined value" for the Professional of \$141/sq.ft.

[50] The Complainant then added \$20/sq.ft. to the \$141/sq.ft figure derived above ("to reflect the subject's higher lease rate than the Professional Building", R.1.-p.3), to derive a total value for the subject property of \$13,868,500 dollars.

[51] In the Complainant's rebuttal submission, they also responded to a time-adjusted sales analysis advanced by the Respondent (R.1.-p.19), noting that while it is not unreasonable to time-adjust the sale, the Respondent erred in deriving a cap rate using the 2009 operating income, rather than 2011 rental rates.

[52] The Complainant proposed adding \$2/sq.ft. to the gross income calculation of the 2009 sale comparable building, increasing the total gross income from \$230,025 to \$259,025, which results in a cap rate for the property of 9.32% - which the Complainant believes supports their contention that while property values may have changed between 2009 and 2011, cap rates did not.

## **Respondent**

[53] The Respondent noted that the only evidence submitted by the Complainant to support their request for an increased cap rate is an "old office building sale" that occurred two years prior to the valuation date of July 1, 2011 (R.1. - p.18), which fails to provide an analysis of current market data in the calculation of cap rates.

[54] The Respondent maintained that in order properly to consider this sale for the purpose of cap rate calculation, the sale must be time-adjusted. The Respondent then included a paired-sales analysis of an industrial building in the north end of the city which sold in October 2009 and again in January 2012, noting a 12.8% increase in price over the 26 month period, or 0.5% per month.

[55] The Respondent argued that applying this 12% increase in value to the 2009 comparable sale property results in a time-adjusted value of \$2,643,200 and a cap rate of 8.27%.

[56] In a rebuttal to the Complainant's rebuttal, the Respondent also submitted a confidential tenant report indicating that the rental rate for this comparable property had not changed over the 26 month period, noting that the rental rate was constant at approximately \$15/sq.ft.

[57] The Respondent further maintained that the City analyzes all non-residential sales on an annual basis in order to apply current cap rates for valuation purposes, and reviews



Capitalization Rate Market Reports prepared by various real estate companies, as well as market report evidence from various sources to monitor cap rates locally, regionally, and nationally.

[58] The Respondent also submitted a chart on p.18 of their submission listing cap rate ranges for different classes of properties in Calgary and Edmonton for the third quarter of 2009 and the second quarter of 2011 – indicating a general decline in cap rates across all categories of these properties for both cities during that time period, ranging from 0.50% to 1.25% down.

[59] The Respondent asserted that the City experienced a similar market decline in cap rates for the 2009 to 2011 time period, and provided two recent office building sales in support of this assertion:

- the Westview Business Centre, sold March 2012 with a cap rate of 7.27%, and
- the Skyway Office Building, sold July 2012 which was 50% vacant at the time of sale, but still sold for more than double its construction costs with a cap rate of 3.5% (or estimated 7% fully rented).

[60] The Respondent further maintained that the City has properly analyzed all relevant data to arrive at an appropriate cap rate of 8.25% for the subject property as of July 1, 2011.

[61] The Respondent concluded by asserting that the Complainant did not provided “any credible evidence” to support a cap rate increase for the subject property. (R.1. - p.19)

### **Board Findings**

[62] With respect to the single sale comparable proffered by the Complainant, the Board finds this sale to be distant in time, necessitating a time-adjustment in order to be meaningfully comparable, and while the Respondent calculated a time-adjusted sale price as of July 1, 2011, they erred in utilizing the 2009 actual net operating income to derive a cap rate for the sale.

[63] If one is going to time-adjust a sale price to reflect changes in an evolving market over time, one must also utilize comparably adjusted income/rental rates to reflect similar changes in the market over the same period when calculating cap rates.

[64] The Board finds, however, that the methodology employed by the Complainant to adjust the income/rental rate for the comparable property is also flawed, since the Complainant used a “market” rental rate increase of \$2/sq.ft. (taken from the increase in “market rent” applied to the subject property by the City from 2010 to 2011), and then applied that increase to the “actual” rental rate for the comparable property of \$15.86/sq.ft.

[65] The adjusted rental rate of \$17.86/sq.ft., therefore, is actually higher than the assessed market rate of \$16/sq.ft. applied to all properties in the high-rise category in down town Red Deer in 2011, and is also higher than the \$16/sq.ft. applied to the subject property’s upper floor office space.

[66] Again, if one is going to time-adjust a sale price, one must ensure to adjust the other factors in determining the cap rate; use market rental rates throughout the calculation, or actual rates throughout. To use “market” rental rates in one instance and “actual” rates in another, is not reasonable property assessment protocol.



[67] Based on the foregoing, the Board is not persuaded that the time-adjustment for the 2009 sale is wholly reliable, and therefore places little weight on the Complainant's reliance on the comparable sale, including all the arguments the Complainant advanced in respect of this comparable.

[68] With respect to the numerous capitalized income calculations the Complainant advanced based upon on a comparison of the subject property to the Professional Building, the Board likewise places little weight on any of these arguments.

[69] The Board accepts the Respondent's assertion that to utilize vacancy/cap/rental rates in the vacuum of one single property and then simply to ascribe these values to the subject property by association is an unreliable methodology for reflecting meaningful capitalization rate principles in a mass assessment environment.

[70] The Board places no weight on the two 2012 sales comparables proffered by the Respondent because they are post-facto the 2011 assessment year.

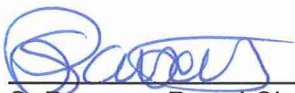
[71] The Board concludes, therefore, that the Complainant provided insufficient persuasive evidence to justify a variance of the cap rate, and therefore confirms the cap rate at 8.25%.

### **SUMMARY**

[72] For the reasons noted above the assessed value of the subject property is hereby CONFIRMED as follows:

Roll #1633735          \$16,978,300

Dated at the City of Red Deer, in the Province of Alberta this 29 day of October, 2012 and signed by the Presiding Officer on behalf of all panel members who agree that the content of this document adequately reflects the hearing, deliberations and decision of the Board.



S. Parsons, Board Clerk on behalf of  
M. Chilibeck, Presiding Officer

**This decision can be appealed to the Court of Queen's Bench on a question of law or jurisdiction. If you wish to appeal this decision you must follow the procedure found in section 470 of the Municipal Government Act which requires an application for leave to appeal to be filed and served within 30 days of being notified of the decision. Additional information may also be found at [www.albertacourts.ab.ca](http://www.albertacourts.ab.ca).**



## **APPENDIX "A"**

Documents Presented at the Hearing  
and considered by the Board

---

**NO.**

**ITEM**

- |       |                                      |
|-------|--------------------------------------|
| 1. C1 | Complainant's Disclosure of Evidence |
| 2. C2 | Complainant's Rebuttal               |
| 3. R1 | Respondent's Disclosure of Evidence  |
| 4. R2 | Respondent's Rebuttal                |

FOR MGB ADMINISTRATIVE USE ONLY

Decision No. 0262-466/2012			Roll No. 1633735	
<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 Method	-Vacancy Rate -Cap Rate -Rental Rate