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**T Update Week 2005-34**  
**Commercial and Industrial Properties**

**Case Name:**

**Hamilton Physicians and Surgeons Buildings Ltd. v.  
Municipal Property Assessment Corp., Region No. 19**

**IN THE MATTER OF Section 40 of the Assessment Act,  
R.S.O. 1990, c. A.31, as amended, and  
IN THE MATTER OF a complaint with respect to taxation  
year 2003 on premises known municipally as 25 Charlton  
Avenue East**

**Between**

**Hamilton Physicians and Surgeons Buildings Limited,  
Assessed Person/Complainant, and  
The Municipal Property Assessment Corporation, Region  
No. 19 and the City of Hamilton, Respondents**

[\[2005\] O.A.R.B.D. No. 475](#)

File No. 40083

Hearing No. 102995

Complaint No. 1513024

**Ontario Assessment Review Board  
I.A. Birnie (Member)**

August 8, 2005.  
(49 paras.)

**Appearances:**

S.M. Pocrnic, for the Assessed Person/Complainant.

F.X. Shea, for the Municipal Property Assessment Corporation.

No one appeared for the Municipality.

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**DECISION**

¶ 1 This complaint came before the Assessment Review Board on March 30, 2005 in the City of Hamilton.

ISSUE

¶ 2 Whether the subject property has been correctly assessed for the 2003 taxation year?

DECISION

¶ 3 The assessment of the subject property for the 2003 taxation year is increased from \$3,771,000 (Commercial \$3,659,000 and Exempt \$112,000) to \$4,151,000 (Commercial \$3,707,710 and Exempt \$443,290).

REASONS FOR DECISION

Description

¶ 4 The subject property is an eight-storey medical office building, with commercial retail and restaurant space on the ground floor, and a parking area, located on a site of approximately 0.69 acres. It has a Gross Leasable Area of approximately 56,081 square feet and a Net Leasable Area of approximately 48,562 square feet. Parts of the property are exempt from taxation because they are occupied by St. Joseph's Hospital.

Existing and Proposed Assessments

¶ 5 The existing assessment of the subject property for the 2003 taxation year is \$3,771,000 (Commercial \$3,659,000 and Exempt \$112,000). This was based on the 1999 base year valuation increased by a factor of 1.3, arrived at by a computer analysis of sales data and market trends, to give the 2001 base year valuation. The complainant seeks a reduction of the assessment to \$2,511,976 (with appropriate breakdown between Commercial and Exempt), made up as follows:

Offices	\$1,918,786
Parking	309,270
Retail	283,920
	\$2,511,976

¶ 6 The Municipal Property Assessment Corporation (MPAC) seeks an increase in the assessment to \$4,151,000, (Commercial \$3,707,710 and Exempt \$443,290), made up as follows:

Offices	\$3,557,810
Parking	309,270
Retail	283,920
	\$4,151,000

¶ 7 Of the assessment of \$3,557,810 on the offices, \$443,290 would be tax exempt as it relates to suites G5, 101, 704, 706/708 and 707 occupied by St. Joseph's Hospital. All subsequent references herein to MPAC's positions and submissions refer to MPAC's positions and submissions in regard to the increased assessment, which it is seeking.

Points of Agreement

¶ 8 The complainant and MPAC agree that:

- a) The subject property should be assessed using the Income Approach.
- b) The subject building is a class "B" building.
- c) The capitalization rate should be 11.00%.
- d) The assessment of the parking area should be reduced from \$387,920 to \$309,270.
- e) The assessment of the retail area should be increased from \$283,500 to \$283,920.

#### Outstanding Issue

¶ 9 The only outstanding issue is the assessment of the office area.

#### Percentage Increase in Assessment of Offices proposed by MPAC

¶ 10 The complainant's agent, Steve M. Pocrnic, protests that the increased assessment of the offices sought by MPAC represents a 51 % increase between the 1999 base year one and the 2001 base year. There is nothing in the Assessment Act requiring any correlation between assessments for different base years. The Board's task is to determine the correct current value for the 2003 taxation year and not to concern itself with assessments for previous years.

#### Determination of Gross Potential Income of the Offices

¶ 11 The complainant's agent, Steve M. Pocrnic, presented a list of the actual office rentals, having a median of \$18.50 per square foot. Mr. Robert Wilson, Senior Valuation Analyst with MPAC, who was accepted by the Board as an expert witness, agreed that the median was \$18.50, but pointed out that the rents were not gross as stated by Mr. Pocrnic, but partially gross, as his inspection of the complainant's lease files showed that virtually all of the leases and rental agreements were on a partially gross basis, with the tenant paying some of the operating expense.

#### Determination of Net Operating Income of the Offices

¶ 12 Mr. Pocrnic testified that the actual expenses for the office area were \$11.95 per square foot, which should be deducted from the \$18.50 per square foot, to give a net market rent of \$6.55 per square foot. On cross-examination, he conceded that the expenses of \$11.95 per square foot included "management" and "leasing commissions" set out in the complainant's financial statement for the year ended January 31, 2001.

¶ 13 MPAC's counsel, Mr. Shea, submitted that deducting the management expenses and then deducting an expense allowance, which is commonly understood to include management cost, was a double count and resulted in understating the fair market rent.

¶ 14 Mr. Shea further submitted that another flaw in Mr. Pocrnic's methodology was including leasing commissions, as Mr. Pocrnic was adopting MPAC's capitalization rate and MPAC did not include leasing commissions when calculating office capitalization rates. Moreover, he submitted that Mr. Pocrnic had erred in deducting all of the operating expenses of the subject property, not just the portion relating to the offices.

¶ 15 Mr. Wilson testified that he had made a detailed analysis of the operating financial statements for fiscal years 2000, 2001 and 2002, and had found the operating expenses to be about \$10.70 per square foot including management expense, and \$9.74 per square foot excluding management expense. He had removed non-applicable expenses shown in the complainant's Financial Statement, namely amortization of tenant alterations, depreciation, mortgage interest and fees, and rent for the parking lot.

¶ 16 The office rents were adjusted to reflect a fully net rental rate, using multiple regression analysis (MRA). The MRA produced a Weighted Mean result of \$9.90 per square foot. As MPAC adjusted the square footage of the offices to use the standard STFA (Single Tenant Floor Area) measurement, a downward adjustment of 15% was made to the \$9.90 resulting in a net operating income of \$8.60, rounded down to \$8.50.

#### Vacancy and Collection Allowance and Expense Allowance for the Offices

¶ 17 Mr. Pocrnic submitted that the net operating income of the offices should be reduced by a vacancy and collection allowance of 20%, and an expense allowance of 10%. He submitted as comparables, five office buildings in downtown Hamilton, which were all afforded a vacancy and collection allowance of 25%, and an expense allowance of 17%, and a medical office building at 1100 Main Street West in West Hamilton, which was afforded a 15% vacancy and collection allowance and an 8% expense allowance.

¶ 18 Mr. Pocrnic's evidence was that most suites were not leased on a long-term basis but rented from month to month, and many of the tenants were elderly, and submitted that this negatively affected marketability.

¶ 19 Mr. Wilson's evidence was that the subject property has a prime location directly across the street from St. Joseph's Hospital, resulting in a very low vacancy rate. The complainant's rent roll dated September 24, 2001 showed three vacant office suites, representing 5.51% of office floor area. His reconstruction of the complainant's Financial Statement for the base year 2001 showed a management expense of 4.78%. In the circumstances, the vacancy and collection allowance of 7% and the expense allowance of 7% allowed by MPAC, were generous.

¶ 20 In regard to Mr. Pocrnic's submissions, Mr. Shea submitted that the owner of an income-producing property with little or no vacancy would not sell at a value reflecting a contrived 20% allowance for vacancy that does not exist. Mass appraisal does not equate to identical valuation assumptions where facts disprove the applicability of such assumptions. The subject property is a medical office building located outside the central business district of Hamilton. It is not in competition with downtown office buildings. The vacancy levels in the downtown core have no relevance to vacancy levels in medical buildings in other areas of the municipality. MPAC does not accept the medical office building at 1100 Main Street West as a valid comparable because of differences in size, condition, design and attributes.

#### Determination of Appropriate Square Footage of the Offices

¶ 21 The complainant's agent submitted that the current value of the offices should be calculated using the Multiple Tenant Floor Area (MTFA) of 46,027 square feet. Mr. Wilson testified that in recognition of the Building Owners and Managers Association International standard of rentable floor area, MPAC used the Single Tenant Floor Area (STFA) (53,546 square feet) for the offices, and to compensate granted a 15% reduction in calculating the net operating income.

#### Valuation of Offices by Income Approach

¶ 22 Mr. Wilson testified that he had reconstructed the complainant's financial statements and had removed non-applicable expenses, resulting in a gross operating income for the offices of \$455,141. Deducting the vacancy and collection allowance of 7% and the expense allowance of 7% gives a net operating income for the offices of \$391,421. Dividing \$391,421 by the capitalization rate of 11 % gives a current value for the offices of \$3,557,810.

#### Total Current Value of Subject Property

¶ 23 Mr. Wilson testified that the total current value of the subject property was as follows:

	Total	Taxable	Exempt
Offices	\$3,557,810	\$3,114,520	\$443,290
Parking	309,270	309,270	NIL
Retail	283,920	283,920	NIL
	\$4,151,000	\$3,707,710	\$443,290

#### Valuation of Subject Property by Direct Comparison Approach

¶ 24 Mr. Wilson testified that while the Income Approach is the best method of assessing income-producing property, he has also valued the subject property by the Direct Comparison Approach. He submitted six medical buildings in Oakville (three), Hamilton, St. Catharine's and Newmarket, which sold between 2001 and 2003 for a median sales price of \$91.66, rounded down to \$90.00 per square foot. Applying this rate to the 48,562 square feet of the subject property, gives a current value of \$4,370,580, rounded down to \$4,370,000. In his opinion, this showed that the assessment of the subject property at \$4,151,000 by the Income Approach is not too high.

¶ 25 Mr. Pocrnic submitted that the sales submitted by MPAC were not good comparables as only one sale was in the base year, and this was in the Town of Oakville, where sale prices are higher. Moreover, several of the sales were of properties which rented for much less per square foot than the subject property.

#### Exempt Portions occupied by St. Joseph's Hospital

¶ 26 The complainant and MPAC agree that the following suites occupied by St. Joseph's Hospital are exempt from taxation. If the assessment of \$3,557,810 on the offices sought by MPAC, is accepted by the Board, the complainant takes no issue with the following apportionments on the exempt suites by MPAC:

Suite G5	\$ 56,970
Suite 101	178,690
Suite 706	101,840
Suite 704	55,260
Suite 707	50,530
	\$ 443,290

#### Legislation

¶ 27 The Board must have regard to section 1, and subsections 19(1), 19.1(1), 19.2(1), 40(11) and 44(2) of the Assessment Act (Act) when determining whether or not the assessment(s) under appeal are correct.

¶ 28 Section 1 of the Act defines current value as follows:

"current value" means, in relation to land, the amount of money the fee simple, if unencumbered, would realize if sold at arm's length by a willing seller to a willing buyer.

¶ 29 Subsection 19(1) of the Act states:

19(1) Assessment based on current value. - The assessment of land shall be based on its

current value or average current value, as determined under section 19.1.

¶ 30 Subsection 19.1(1) of the Act provides:

19.1(1) Assessment, single years and averages. - Subject to subsections (2) and (3), land shall be assessed for a taxation year at the current value of the land for the taxation year.

¶ 31 Section 19.2(1) of the Act provides:

19.2(1) Valuation days - Subject to subsections (2) and (5), the day as of which land is valued for a taxation year is determined as follows:

1. For the 1998, 1999 and 2000 taxation years, land is valued as of June 30, 1996.
2. For the 2001 and 2002 taxation years, land is valued as of June 30, 1999.
3. For the 2003 taxation year, land is valued as of June 30, 2001.
4. For the 2004 and 2005 taxation years, land is valued as of June 30, 2003.
5. For the 2006 and subsequent taxation years, land is valued as of January 1 of the year preceding the taxation year.

¶ 32 Subsection 40(11) of the Act states:

40(11) Board to make determination - After hearing the evidence and the submissions of the parties, the Board shall determine the matter and, in complaints involving current value, shall determine the amount of the assessment as necessary to reflect corrections to the current value.

¶ 33 Subsection 44(2) of the Act states:

44(2) Reference to similar lands in the vicinity. - In determining the value at which any land shall be assessed, reference shall be had to the value at which similar lands in the vicinity are assessed.

Case Law submitted by Complainant's Agent

¶ 34 Mr. Pocrnic submitted the following Assessment Review Board cases for the Board's consideration:

- (a) 802700 Ontario Inc. v. Municipal Property Assessment Corp., Region No. 19 [\[2003\] O.A.R.B.D. No. 68](#) (ARB File No. 20572)

In this case, MPAC took the position that it was appropriate to consider what is typical in the market in terms of rent and vacancy rates, etc., but Board Member S. Campbell made no findings in this regard and held that the best evidence of value in this case was a sale of the subject property.

- (b) Icorr Properties Inc. v. MPAC, Region No. 23 [\[2002\] O.A.R.B.D. No. 414](#) (ARB File No. 14406)

In this case regarding the valuation of office and rental buildings in London, Board Members R. Whitnall and T.S. Birtch stated at page 4, para. 5:

5. The Board finds that the fairest and most accurate method of determining income for this type of property is to deduct allowances for industry-wide averages for expenses and vacancy rates from actual gross potential income, and to multiply that result by a standard capitalization rate established from actual sales ...

and at page 5, para. 31:

31. The Board also finds that the actual rental data of the subject property by themselves did not accurately reflect market rental rates as of the base date ... The Board approves of MPAC's resort to comparable competitive properties and other market sources of rental data as well as actual net rents of the subject property to determine fair market rents ...

- (c) Harris Drug Store Ltd. v. Ontario Property Assessment Corp., Region No. 28 [\[1999\] O.A.R.B.D. No. 322](#) (ARB File No. WR 98-292)

In this case regarding the valuation of a medical/dental office building in North Bay, Member R. Butterworth held that the best comparisons were not general commercial and retail properties, but other medical/dental buildings. He also found that as the main floor tenant was not at arm's length from the complainant and as the main floor rent had been negotiated in 1990 when the North Bay economy was more robust, the use of reasonable rather than actual revenue would result in a more correct current value.

Case Law submitted by MPAC

¶ 35 Mr. Shea submitted the following cases for consideration by the Board:

- (a) Re A. Merkur & Sons Ltd. and Regional Assessment Commissioner, Region No. 14 et al., (1977) [17 O.R. \(2d\) 339](#) (H.C.J.)

This Ontario High Court of Justice Divisional Court case was an appeal from the decision of the Ontario Municipal Board regarding a shopping centre in the Town of Aurora. The judgment of Justices Hughes, Rutherford and Steele states at page 3, lines 26/28:

The best that can be achieved is to compare the value of the property in

question by some standards to the best known evidence of the market place and, based on this, attempt to arrive at a figure that is fair, not only to the property owner and the municipality, but also to all other property owners within the municipality.

and at page 5, lines 39/40:

... reference should, wherever possible, be made to other methods of appraisal to confirm the income appraisal made.

- (b) *Hotel Toronto v. Regional Assessment Commissioner, Region No. 9 et al.*, (1980) 11 O.M.B.R. 170 (O.M.B.)

This Ontario Municipal Board case was heard by Members Shub and Henderson, and their decision at page 172, lines 3/9 states:

In this case, the original assessment as made by the assessor was arrived at by a different and earlier utilized method. It is our opinion that the Board must be concerned not by a similar application of technique, but we must consider the final assessment as made ...

- (c) *Cogan v. Municipal Property Assessment Corporation, Region No. 3 et al.*, (22 July, 2004) (unreported) File No. DM 2084 (ARB). In this Assessment Review Board case, Board Vice Chair J. de P. Seaborn stated:

... the issue is the correct current value for the property under appeal and not whether the model used by MPAC to arrive at values is correct. Simply put, the model relied on by MPAC is a valuation tool and not a requirement of the Assessment Act. It is not the particular model that is to be tested on appeal, rather it is whether the current value of the property is incorrect ...

- (d) *Flett v. Ontario Property Assessment Corp., Region No.10*, [\[2000\] O.A.R.B.D. No. 903](#) (ARB File No. 1822) Board Member (now Chair) R.F. Stephenson stated on page 1, para. 3:

The Board finds that the MRA model is only a tool by which OPAC endeavours to determine the current value of properties. Similarly, any other model is only a tool and is not determinative by itself, of correct current value. The complainants must show, by reference to the subject properties value and by reference to the assessments of similar properties in the vicinity, what the correct assessment of the properties should be.

- (e) *Kelly v. Ontario Property Assessment Corp., Region No. 9*, [\[2001\] O.A.R.B.D. No. 685](#) (ARB File No. 6532)

In this Assessment Review Board case, Board Member E. Justin states at page 3, para. 20:

20. With respect to the appraisal methodology known as MRA and to which the complainants' counsel took exception, the Board expresses the view that by whatever name a valuation system is called, it is only the resulting end figure as an opinion of value that is the ultimate testing point and which needs to be proven or disproven. It is not the system of evaluation itself which needs to vindicate itself. Any disparaging of MRA as a method of evaluation merits less weight to the Board in arriving at its deliberations than the provision of definitive evidence leading to the establishment of a current value as of the base year required.

- (f) 3100 Steeles Avenue West Investment Inc. v. Municipal Property Assessment Corp., Region No. 14, [\[2002\] O.A.R.B.D. No. 622](#) (ARB File No. 14411)

In this Assessment Review Board case, Board Member B. Cowan states at page 3, para. 18:

... the Act does not stipulate the methodology for valuation. Further, ... the Board is not restricted in choosing a basis to establish an assessed value. The Board must evaluate the evidence and argument presented, and is obligated to establish a current value ... based thereon.

and at page 3, para.22:

For purposes of establishing current value, the Board ... has no directive from the Act respecting similarity or vicinity. These concepts may, of course, be significant in valuations using a sales comparison methodology. But the possible current values may be demonstrated by any means that parties to complaints choose to advance.

#### Findings by the Board

¶ 36 Having regard to the case law submitted by the complainant's agent, the Board finds that the best method of valuing an income producing property is by the income method using market rents and typical vacancy and expense allowances, where there are truly similar properties in the vicinity from which such data can be learned.

¶ 37 The Board finds that in this case there are no similar properties in the vicinity that are truly comparable to the subject property, which is a medical office building outside the Hamilton downtown core and has a prime location directly opposite St. Joseph's Hospital. The subject property cannot be compared to office buildings in the downtown core, which have high vacancy rates compared to the subject property's very low vacancy rate, and it cannot be compared to the one other medical office building submitted by the complainant's agent as the building at 1100 Main Street West is in West Hamilton and is not close to a hospital.

¶ 38 The Board finds that MPAC is not required to use the same methodology in valuing the offices as it uses to value office buildings in the downtown core or the medical office building at 1100 Main Street West. As held in the cases submitted by MPAC, the issue is not whether MPAC's methodology is correct, but whether the assessment sought by MPAC is correct.

¶ 39 The Board finds that in this case where there are no truly comparable properties and where almost all the rents are from month-to-month leases, it is appropriate for MPAC to use the actual rents and expenses in its valuation of the offices.

¶ 40 The Board prefers Mr. Wilson's calculation of the net operating income of the offices at \$8.50 per square foot to Mr. Pocrnic's calculation. The Board finds Mr. Pocrnic's calculations to be flawed for the following reasons: (a) he treats the actual rents as gross when most are only partially gross, (b) he deducts actual management expense as well as an expense allowance, (c) he deducts leasing commissions, which were not used by MPAC in adopting the capitalization rate, and (d) he deducts all of the operating expense, not just the portion relating to the offices.

¶ 41 The Board finds that the vacancy and collection allowance of 7% and the expense allowance of 7% used by MPAC are appropriate and are greater than the actual percentages for the offices. It would unduly lower the valuation of the offices to use the rates which were used for downtown office buildings or for the medical building at 1100 Main Street West. The Board is satisfied that the capitalization rate of 11%, agreed by MPAC and the complainant, to be appropriate.

¶ 42 The Board finds that MPAC's use of the Single Tenant Floor Area (STFA) of 53,546 square feet is appropriate, when coupled with the 15% reduction used in calculating the net operating income of \$8.50 per square foot for the offices.

¶ 43 The Board accepts Mr. Wilson's calculation of the current value of the offices at \$3,557,810, although mathematically dividing the net operating income of \$391,421 by the capitalization rate of 11% gives \$3,558,372.

¶ 44 The Board notes that if the Multiple Tenant Floor Area (MTFA) of 46,027 square feet were used, as advocated by Mr. Pocrnic, the product of multiplying the MTFA by the net operating income of \$9.90 would be \$455,667. Deducting the allowances of 14% gives \$391,874 and dividing by the capitalization rate of 11% gives a current value of \$3,562,490 for the offices, which is \$4,680 more than the value calculated by MPAC.

¶ 45 The Board places no weight on the calculation of the value of the offices by MPAC using the Sales Comparison Approach as the comparables used by MPAC were disputed by the complainant's agent and as MPAC and the complainant's agent agreed that the Income Approach was the correct method of assessment.

¶ 46 The Board finds that the parking area is correctly valued at \$309,270, as agreed by MPAC and the complainant. The Board finds that the retail area is correctly valued at \$283,920, as agreed by MPAC and the complainant.

¶ 47 Accordingly, the Board finds the total value of the subject property to be as follows:

Offices	\$3,557,810
Parking	309,270
Retail	283,920
	\$4,151,000

¶ 48 The Board finds the value of the exempt offices occupied by St. Joseph's Hospital to be \$443,290, as agreed by MPAC and the complainant's agent.

¶ 49 The assessment of the subject property for the 2003 taxation year is increased from \$3,771,000 (Commercial \$3,659,000 and Exempt \$112,000) to \$4,151,000 (Commercial \$3,707,710 and Exempt \$443,290).

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