TURNER DRAKE + PARTNERS

newsletter

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Update

A number of readers phoned or wrote to us after the first issue of Newsletter in March. We would like to thank them for their comments and encouragement. Especially welcome were the suggestions for future articles. Suggestions so far include: MURB's; Investment Opportunities for the Small Investor; the Cost of Appraisal and Consulting Services; and the new Assessment Act.

Two new beards joined our Company in April, John d. Morehouse, B.Sc., and Richard Leonard, C.R.A. John specializes in commercial and industrial appraisals, while Richard takes control of our Residential Appraisal Department.

We can now claim the somewhat dubious distinction of being the Atlantic Provinces' most completely whiskered firm of real estate consultants. Our secretary is too kind to comment, but no doubt Freud had a word for it.

Beware the Ides of March

As the assessment rolls closed in Halifax/Dartmouth, it became apparent that the new provisions of the Assessment Act were about to take their toll.

With increasing inflation over the past few years, there has been a swing to net net leases. Often, it is the tenant who now bears the brunt of any increase in real estate taxes. This is compounded by the fact that the Occupancy Tax is now directly related, throughout the Province, to the assessed value. In some Municipalities - the City of Dartmouth is an example - this is a complete change from previous years.

Unfortunately, in the case of a multi-occupancy building such as an office tower, shopping centre, etc., there is little an individual tenant can do unless he is willing to appeal the assessment on the entire property. The Landlord may have little or no incentive to appeal the assessment because he is protected through tax escalation clauses in his leases. The past few months, therefore, have seen the emergence of a new trend as tenants band together with the landlord to appeal the real estate assessment on the entire property, whilst individually they appeal their own occupancy assessments.

Income - The Forgotten Approach

Pity the poor Assessor. If he is conscientious in assessing the property at its full cash value, as required by the Assessment Act, he gets little thanks from the taxpayers as a whole but suffers the opprobrium, and often abuse, from the individual property owner. Almost as popular as the folks from Revenue Canada, he has to complete his work, often with a minimum of co-operation from the individual property owner.

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suite 703 1888 brunswick street halifax n.s. b3j 3j8 tel (902) 429-1811

Due to the volume of work and the reluctance of property owners to disclose the rental rolls and operating statements for their buildings, Assessors rely in the main on the Cost Approach to Value. This is the value arrived at by aggregating the land value and the cost of reproducing the building. The latter is calculated by estimating the cost of building the structure and deducting therefrom obsolescence due to Physical, Functional and Economic causes.

Physical Obsolescence, i.e. depreciation from wear, tear and age, is usually visible and therefore apparent on inspection.

Functional Obsolescence, i.e. the inability of the property to meet modern requirements of layout, ceiling height, etc., is likewise also apparent to an experienced eye.

Economic Obsolescence, i.e. the failure of the property to compete successfully due to external causes, e.g. oversupply, changes in demand, can usually only be quantified by studying the income and expense statements.

When the economy is booming, rising demand and inflation often mask Economic Obsolescence. However, at the present time, market demand is soft for almost all types of real estate. There is an excess supply of retail and office space in the Halifax/ Dartmouth Metropolitan Area. The supply and demand curves for office space, for example, will not be in equilibrium for another three years or so. Retail space, always susceptible to competition from new centres in interceptive locations, may never be fully utilized. These properties are suffering from Economic Obsolescence and are prime suspects for over assessment.

The explosion in hotel rooms in the area, during the boom period which ended at the beginning of 1976, has resulted in low occupancy rates. Since hotels have high fixed costs, they require occupancy rates of about 70% to break even. Any shortfall in occupancy rapidly translates itself into low residual cash flows and consequent lowering of the property value.

The older apartment buildings and rooming houses, too, are feeling the competition from newer buildings erected with the aid of Government subsidies (limited dividend) or under the MURB program. Couple this increase in supply with rent control, a rapid increase in operating costs, particularly insurance, heating and electricity, and you have an accelerated rate of obsolescence which may not be apparent unless the financial statements are available.

What to do

The Assessment Act states that the property has to be assessed at its actual cash value. This is defined as the price it would bring if sold at auction. There is a caveat that regard has also to be had to the general level of the assessments in the Municipality. Thus, the 1978 assessment might actually relate back to an earlier base date cost and value level (January 1976 in the case of the City of Dartmouth).

If you know that the financial state of the property is less rosy than physical appearances would suggest, there is a good chance that an appeal is warranted. Any appraisal firm will advise you as to whether the appeal is justified.

The Residential Scene

Due to space limitations we have deferred the remainder of the Residential Scene article, contained in Volume 1 Number 1 of Newsletter, to a later issue.