TURNER DRAKE & PARTNERS
Real Estate Counsellors, Brokers & Valuers

Newsletter

Turner Drake & Partners Ltd.
6182 North Street,
Halifax, N.S.
B3K 1P5
Tel: (902) 429-1811
Toll Free: (800) 567-3033
Fax.: (902) 429-1891
E-Mail: tdp@turnerdrake.com
Internet: www.turnerdrake.com

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WHO VALUES US NOW?

(Photograph courtesy of SunDancer Photo Communications)

The decision by Canada's appraisal industry, or those of them that are members of the Appraisal Institute of Canada, to abandon the "USPAP" international appraisal standard (Newsletter Vol. 2 No. 68) creates a dilemma for property owners who want the assurance that the appraisal they commission will have credibility at home and abroad. Unless an appraisal report has "legs" i.e. wide acceptance within the circle that expects to rely upon it; the report is worthless … no matter how little it costs.

USPAP (Uniform Standards of Professional Appraisal Practice) was universally adopted throughout the United States in 1989 as a response to the Savings and Loan scandal that almost brought that country's financial system to its knees. Had not the Federal Government intervened it is likely that the United States' economy would have collapsed, triggering the failure of the global financial system in its wake. USPAP, and its administering body, The Appraisal Standards Board of the Appraisal Foundation in Washington, D.C. were a Federally mandated initiative to ensure that a similar situation would not occur again. Although Canada suffered its own financial crisis, based on inadequate appraisal practices, which resulted in the loss of most of its Trust Companies, and several Life Insurance Companies, government action here was muted largely because of the division of legislative authority. As a result we have lost control of much of our major property financing. Increasingly it has passed into the hands of American conduit specialists such as Merrill Lynch, GMAC, etc. We expect this trend will continue to grow. Since the mortgage bonds are raised and rated in the United States market appraisals have to meet USPAP standards … nothing else "cuts" it.

USPAP was adopted by the Appraisal Institute of Canada (AIC) in 1994 only after the Canadian Insurance Deposit Corporation (CIDC), tired of waiting, introduced its own appraisal standards. USPAP was greeted with a noticeable lack of enthusiasm: Canadian appraisers grumbled that clients would not pay for the extra work and effort involved. On January 1st 2001, a scant six years later, the Appraisal Institute of Canada abandoned USPAP and introduced its own "Canadian Uniform Standards", rather misleadingly marketed as the "Canadian version of USPAP" approved by the "Appraisal Standards Board". The latter refers not to the independent board that administers USPAP, but apparently is really the AIC itself. The "Canadian Uniform Standards" have not been approved by the Appraisal Foundation, are a creature of the Appraisal Institute of Canada and replace the objective standards of USPAP with a "reasonable appraiser" test instead. Appraisals that no longer need to conform to USPAP are cheaper … we estimate that they can be completed at about half the cost … so the obvious question is why not?

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Why Not, Indeed?

USPAP's strength is that it is grounded in reality … it effectively killed the practice of blithely formulating values without adequate research, and thence limiting liability with a host of escape clauses disclaiming responsibility for checking the leases, operating expenses, floor areas, zoning, planning, assessment … or even that the property existed "on the ground". Prior to USPAP many appraisals assumed a set of fiscal, physical and legal conditions that were unverified … and often did not exist. Of course USPAP did not eliminate the practice of hypothetical appraisals, but by providing a set of standards that the Courts could rely upon, they did afford judicial relief when a party suffered loss … and they placed constraints on the practice. USPAP was particularly effective in expropriation cases. Acquiring authorities have a lamentable habit of commissioning appraisal reports "for negotiation purposes" which often fail to address the total loss suffered by the unfortunate property owner. The Courts, armed with USPAP, accorded them the respect they deserved … and many property owners were able to avoid legalised theft.

Horses for Courses

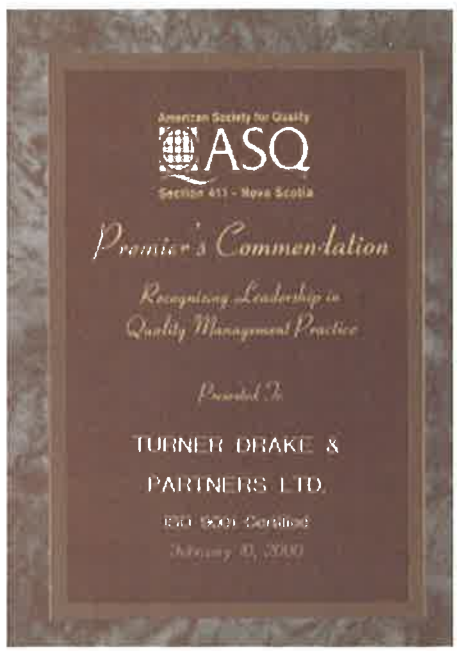
If USPAP's greatest strength is its insistence on reality, its secondary principle is transparency. Clients require property valuations for a variety of purposes … some of which demand a high degree of accuracy and due diligence … others are required only as an input to broad decision making and are of a preliminary nature. USPAP is sufficiently flexible that the assignment can be tailored to the client's needs provided the valuation report clearly identifies the parameters of the assignment. We have taken advantage of this flexibility by developing six valuation products, each precisely tailored to your requirements; financial and operational. Since there may be occasions when you will be satisfied with an appraisal prepared to the Canadian Uniform Standard (CUS) rather than USPAP, we have also developed this appraisal product. The various products are shown in the table. For ease of reference, we have listed the type of report, function, intended end user and the standard (USPAP or CUS) to which each complies. We have chosen to retain the USPAP standard for most of our work since it has widespread acceptance throughout Canada and is the only standard accepted in the United States. We have a strong litigation practice too and Canadian courts increasingly rely upon USPAP to determine whether a real estate appraisal passes evidentiary muster.

We have also listed the relative cost of each type of assignment, using a 50,000 ft.^{2} warehouse valuation, for cost comparison purposes.

Type	Function	End User	Standard	*Cost (%)
Master Valuation Report	Provides end user with a comprehensive (fiscal, physical, and legal) picture of the property. Invaluable resource document for asset management.	**Unlimited**. Conduit financiers eg. GMAC, Merrill Lynch, etc. "Court ready" report for expropriation, capital gains tax, assessment appeals, etc.	USPAP	100%
Valuation Report	Complete valuation in summary format. Used for all property types unless the purpose of the assignment is to litigate a dispute.	**Unlimited** apart from "conduit" financiers and litigation.	USPAP	75%
Form Valuation	Complete valuation in summary format. We usually issue this report on smaller properties.	**Unlimited** apart from "conduit" financiers and litigation.	USPAP	58%
Certificate of Value	Complete valuation issued in restricted format. The report contains a statement of our findings and conclusion but our notes and working papers are held on file rather than being included in the report.	**Limited** to client.	USPAP	55%
Appraisal Report	Appraisal report undertaken in accordance with the Appraisal Institute of Canada's Uniform Standards.	**Untested**. According to the AIC, the Canadian Uniform Standard has been approved by the Canadian banking system for mortgage financing.	CUS	52%
Update Valuation	This type of valuation is the most economical way to proceed if there is a requirement for periodic revaluations of the property.	**Limited** to client.	USPAP	29%
Letter of Opinion	This is a limited valuation and is generally based on an external inspection of the property and such information as is available in our Data Bank. It provides a value range and a "most probable" value.	**Limited** to client. This type of valuation is of a preliminary nature only, to be used as an input to broad decision making.	USPAP	25%

*Note: Cost comparison is based on a 50,000 ft.^{2} warehouse.

RECIPIENT OF PREMIER'S COMMENDATION! Oo-La-La!



On November 23rd last year, we received the Premier's Commendation,

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Recognising Leadership in Quality Management Practice at the American Society of Quality's annual dinner (we forgot to mention it in our last Newsletter; oops!). Thank you Dr. Hamm ... and that despite the nasty things we say about politicians ... would that your simple servants were as generous.

Not that we were alone, mind you. The same award was also presented to forty-one Nova Scotian firms whose quality systems were newly registered to the ISO 9000 quality standard. We were in illustrious company: Stanfield's, Xwave Solutions, Siemens Westinghouse, Mactara Limited, Trenton Works Ltd. Railcar, ... to name but a few. Patti Farewell and Mike Turner accepted the award on behalf of TDP. Thanks guys, it was and continues to be a great team effort.

The recognition apart, the most impressive part of the event for us, was the adoption by so many local firms of the international ISO 9000 quality standard. We believe this is just the beginning. Although it is **the** quality standard in the European Economic Community and has been adopted in 130 countries worldwide, it appeared late in North America. United State's firms exporting into the EEC found it necessary to achieve ISO 9000 registration to remain competitive. Canadian companies selling into the U.S. and the EEC followed suit. Ford, Chrysler and General Motors have adopted a variant of it ... three local Chrysler dealerships (Blaikes Dodge, Scotia Chrysler, Dartmouth Dodge) were year 2000 registrants ... and in our humble way we have set a trend in the real estate industry. When we received ISO 9000 registration in February 2000, we were the only company in our field in Atlantic Canada. We understand that at least three other real estate brokers in the region are now in the process of implementing ISO 9000. We wish them well.

Why ISO 9000?

We believe that history will record the 1990 global recession as a watershed: it forever changed the way business defined its role. *The single most significant trend is the decision by the private and public sectors to focus on their core competencies and to outsource all other activity.* This trend is now well developed in the private sector, primarily manufacturing, but is also evident in the privatisation of many hitherto public sector activities. The trend is also developing in the private sector in areas outside manufacturing, as businesses everywhere focus on what they do best.

We studied companies such as General Electric, Virgin Group, Dell Computer, et al, to determine the strategies they employ for successful outsourcing. Our research revealed that three basic conditions must be met by the outsourcee: one of those was consistent quality.

The ISO 9001 quality standard consists of twenty elements governing all of the activities of our company: everything from the initial contract to provide the service, the control (including confidentiality) of customer supplied information, process control, testing of the service during the various stages to ensure that it conforms to the quality standards, and final delivery. The ISO 9001 quality standard ensures traceability, accountability, and management review, throughout the service delivery process. We were particularly interested in its application to real estate valuation and appraisal since confidentiality is a major concern to clients commissioning this type of service ... and also because appraisal is a "cottage industry" in Canada, and there is no effective control over work standards. *A valuation opinion without adequate research, is valueless.*

Our ISO 9001 quality system is monitored for conformance semi-annually by a system of internal audits which cover every ISO 9001 element, in each area of the company, over a twelve month period. QMI, our external auditors, undertake a surveillance audit every twelve months and a re-registration audit every thirty six months. They completed their surveillance audit early this year and gave us a clean bill of health.

Cut Your Costs and Risk

Your costs of monitoring and verifying that the services and products you purchase, meet contract specifications, adds between 10% and 25% to the price. If the service or product has to be returned and/or resupplied this cost escalates substantially. If you are given wrong advice because of, for example, an inadequately researched appraisal, your costs disappear out of sight. When a supplier conforms to the ISO 9000 quality standard you can avoid the cost and most of the risk of receiving a sub-standard product. Quality becomes our cost, not yours.

INTERNET

Your Real Estate Oracle Version 2.0

We spend much time studying our navels (not a pretty sight) and those of industry leaders Dell Computer, General Electric, Virgin Group, et al, in the hope that such an exercise will lead us to the Holy Grail ... and thence fame and fortune. This navel gazing has convinced us that the one enduring trend to emerge from the 1990 recession will be the elimination of peripheral activity by businesses in favour of a focus on core competency. Peripheral activity such as real estate will be outsourced instead (we hope) to firms such as ourselves. New America International (NAI) was a pioneer in the real estate field. They spotted the emergence of this trend in the late 1980s (Newsletter Vol. 2 No. 67) before it was given impetus by the 1990 recession.

Our studies of industry leaders in outsourcing indicate three criteria which are pre-requisites to successful outsourcing. One of these is consistent quality, hence our decision in 1998 to invest in an ISO 9001 registered quality system and its certification in February 1999. *A second criteria is the integration*

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of the outsourcee's activities into the outsourcer's supply chain management system. The Internet has emerged as the vehicle of choice.

Microforum has just completed the first upgrade of our web site **www.turnerdrake.com** … part of a continuing effort to make it **your** web site. In addition to updating 50% of the present site to provide you with current information on property tax, expropriation case law, market intelligence, etc. we've added FAQs (frequently asked questions) on Lasercad™ space measurement ... the answers too. Most importantly, we've taken the web site one step further as a B2B (business to business) tool by adding a Client Area. This will allow you to integrate our activities into your own by providing you with a password protected area specific to your company. There you will be able to check, on an individual property basis, the status of every assessment appeal, fire insurance report, valuation update, proposed planning and zoning change, Lasercad™ assignment ... and the progress of all sale or leasing projects we are undertaking for you. You can now order assignments on-line, monitor their status, control the assignment … even review past assignments in your property portfolio.

PROPERTY TAX DIVISION

Nova Scotia

Brownlow Avenue, Dartmouth, N.S.
($69,000/annum – 38% in tax savings)

Commercial Realty Taxes to Rise by 32%?

The Nova Scotia government continues its desperate search for more tax revenue. It has no choice. Like its predecessors, it has eschewed "radical" solutions such as the privatisation of government agencies such as the Liquor Commission … though in truth the province may be the only place left on the globe where such solutions would be considered controversial. The politicians are eunuchs: in thrall to the civil service unions, wherein the true power lies. Twas ever thus, so raising taxes it must be … everything is on the table. This year the province downloaded the cost of their Assessment Department onto the municipalities … whilst continuing to raise the monies through the income tax … and then instituted a "user fee" for taxpayers requesting assessment information.

Now realty taxes are under attack. The province proposes to reduce the cost of the assessment process by rolling the Business Occupancy Tax into the Realty Tax. By eliminating Business Occupancy assessments they estimate that they will be able to reduce their costs by the equivalent of six full time positions. The municipalities will benefit too: Business Occupancy is a "leaky" tax, difficult to police and often, to collect. The effect will be to increase the various realty tax rates by the amounts shown in the Realty Tax Table.

REALTY TAX INCREASES		
Major Municipalities	**$ Increase in Commercial Tax Rate**	**% Increase in Commercial Tax Rate**
Cape Breton Regional Municipality	$1.157	29.3%
Halifax Regional Municipality	$1.011	26.1%
Queens Regional Municipality	$0.738	28.9%
Amherst	$1.074	31.6%
Bridgewater	$0.904	31.6%
New Glasgow	$1.117	32.8%
Truro	$1.025	31.5%
Yarmouth	$0.859	28.4%
Colchester County	$0.494	25.9%
Guysborough County	$0.758	48.9%
Kings County	$0.449	26.2%
Pictou County	$0.468	34.9%
Richmond County	$0.478	35.9%
Total All Municipalities		31.8%

Source: Province of Nova Scotia, Discussion Paper Concerning Business Occupancy Assessment and Taxation; February 2001.

Tax Take

Although the total tax burden should not increase substantially; it will be redistributed. Currently Business Occupancy assessments are based on the following percentage of the property's Realty assessment:

% of Realty Assessment	Type of Business
25%	Service Station, Restaurant, Campground, Trailer Park, Motor Vehicle Dealer, Hotel/ Motel.
75%	Bank, Credit Union, Loan Company, Trust Company, Insurance Company, Investment Dealer, Mortgage Broker, Collection Agency.
50%	Everybody else.

Source: Province of Nova Scotia, Assessment Act; 1989.

The general impact of rolling the Business Occupancy tax into the Commercial Realty tax, all else being equal,

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will be as follows:

(1) All businesses in the 75% bracket, i.e. financial institutions, will pay less tax.

(2) All businesses in the 25% bracket will pay more tax. Seasonal, tourist related businesses, i.e. restaurants, campgrounds, hotels/motels, will be particularly hard hit since at present they only pay Business Occupancy Tax for the months they are open (usually five months per year).

(3) Businesses in the 50% bracket should be tax neutral.

(4) Commercial landlords will pay 32% more tax unless they are able to recover the excess from their tenants, for example through "net absolute leases", or because of legislated "transitional" arrangements.

(5) It will be much more "risky" to own commercial property since the owner will effectively pay Business Occupancy Tax on all vacant space.

*For more information on the proposed change to Business Occupancy tax visit the Province of Nova Scotia's web site at **www.gov.ns.ca/snsmr/muns/busocc-tax/**.*

New Brunswick – Break and Enter

Hughes Street, Fredericton, N.B.
($12,250/annum – 51% in tax savings)

Our New Brunswick tax team are a keen bunch. Six foot chain link fences topped with three strands of barbed wire are but a minor challenge … properly attired in pin-stripes too, you'll notice … one has to keep up appearances, even when engaged in the odd break and enter. Such dedication has its rewards. We've saved clients millions of dollars; money that falls directly down to their bottom line. And we are hard at work in the province right now. The Year 2001 appeal period ended on March 31st so if you did appeal, but have not yet contacted us, call Tom Mills, André Pouliot or Mike Turner at 1-800-567-3033.

The provincial Assessment Department, a.k.a. Service New Brunswick, took aim this year at the pulp and paper industry. Other types of heavy industry area are scheduled to be re-assessed in 2002. The impact on the pulp and paper industry is dramatic, as the accompanying table starkly demonstrates:

Mill/Location	Assessment			Percent Increase '00 to '01
	1992	2000	2001	
Nexfor Inc. (Frasers) Edmundston	$34,677,500	$56,081,000	$65,479,700	16.8%
Irving Pulp & Paper Saint John	$38,437,400	$38,437,400	$58,711,200	52.7%
Irving Paper Ltd. Saint John	$45,050,800	$45,693,700	$69,978,500	53.1%
Lake Utopia Paper (J. D. Irving) St. Georges	$3,016,900	$3,092,500	$12,685,000	310.2%
St. Anne-Nackawic Nackawic	$19,661,800	$22,964,900	$44,376,100	93.2%
Smurfit-Stone Bathurst	$39,103,800	$39,165,400	$40,528,200	3.5%
AV Cell Inc. Atholville	$20,925,700	$19,384,300	$36,900,700	90.4%
Bowater Maritimes Dalhousie	$31,046,400	$30,696,000	$53,654,500	74.8%
Repap New Brunswick Alcell Plant	$7,379,300	$1,698,500	$1,698,500	0.0%
UPM-Kymmene Miramichi (Total)	$117,681,200	$119,575,600	$190,395,800	59.2%
Total	$356,980,800	$376,789,300	$574,408,200	52.4%

The downturn in the economy, and concomitant decrease in profitability of this highly leveraged, capital intensive industry adds salt to the wound. 2000 was not a great year economically, 2001 promises to be worse … and increases in the industry's aggregate tax bill of 52% are not helpful. The province's actions threaten to kill the goose that laid the golden egg.

Aim Low, Hit Hard

The provincial Assessment Department first adopted its aggressive stance towards heavy industrial properties in the early 1990s. Then rather ominously known as the Geographic Information Corporation, this Orwellian sounding entity successfully defended the inclusion of equipment power wiring as an assessable component of special purpose buildings such as pulp mills before the N.B. Court of Appeal *(Miramichi Pulp and Paper Inc. 69/95/CA)* Renamed Service New Brunswick in the late 1990s, the Assessment Department has a friendlier face today befitting its new name. Nonetheless it continues to savage heavy industry and has taken the position in ongoing litigation that equipment foundations are assessable too. They won the assessment appeal at the Regional Assessment Review Board *(Noranda Inc. versus Director of Assessment, Assessment Appeals 1994, 1995 & 1996. North Esk LSD Property Account No. 02763874. March 30th 1999)* but the Board decision was ambivalent on the critical point of

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equipment foundation assessability. The decision was appealed and heard by the N.B. Court of Queen's Bench in the Spring of 2000 and the question of equipment foundation assessability was argued before the Court. The latter issued their decision on April 17th. Now, we are great believers in the Canadian justice system, even when, as in this case we are on the losing side. However this was not their finest hour. After a full year of deliberations the Court of Queens Bench decided ... (drum roll) ... to make no decision. Oh dear. Back to the drawing board.

We'll keep you informed.

Prince Edward Island

Year 2001 Assessment Notices were mailed on May 4th. The legislated basis for your assessment is the market value of your property as at the 1st January 2001. Unfortunately there is no "uniformity" provision in the Assessment Act so if, as is usually the case now in the Province, you are assessed at less than market value, you are deprived of grounds for appeal ... even if your assessment is too high compared with similar properties. However it has been our experience that the assessors are somewhat sympathetic to the concept of uniformity so if you are unfairly assessed, file an appeal. The appeal period closes on June 18th.

Tom Mills or Mike Turner (1-800-567-3033) are available for free telephone consultation.

For more information on Property Tax case law visit our web site ***www.turnerdrake.com*** *and follow the links (products → property tax → case law).*

THE PRE-MILLENNIUM MELTDOWN – A RETROSPECTIVE

In an earlier article (Newsletter Vol. 2 Nos. 65, 66, 67) we took a look at the Wharton study on the 1990 global property crash and added the knowledge we had gained from studying its effects in Atlantic Canada. So it was with some interest that we received, via the Internet, a study by Tanya Pierson entitled "Why Hotel Markets Crash". Tanya is Senior Vice President of Finance at HVS International, the world's largest appraisal and consulting company solely devoted to the hospitality industry. Tanya studied the Salt Lake City hotel scene during its current run up to the February 2002 Olympics.

The Hotel Valuation Index (HVI) published annually by HVS International showed the following actual and projected declines in Salt Lake City hotel values:

Year	Decline	Comments
1998	26%	Actual
1999	37%	Actual
2000	25%	Projected
2001	17%	Projected
2002	11%	Projected
2003	9%	Projected

Tanya's study found that this loss in value was due to a combination of the following factors:

(1) An expansion in supply as hotel operators built in anticipation of the Olympics.
(2) Reduction in demand due to the closure of primary exits off Interstate 15 as road construction occurred preparatory to the Olympics.

She reasons that property market crashes are usually due to a combination of events:

(1) Supply growth.
(2) Demand reduction.
(3) A negative event.

The negative event is really a sub-set of supply growth or demand reduction and is the "trigger" causing the reduction in demand or expansion in supply.

For more information on HVS and this article visit their web site at ***www.hvsinternational.com*** *and follow the links (articles → Boulder → Why Hotel Markets Crash).*

VALUATION DIVISION

V-Day Values for Capital Gains Tax

We've been in business for twenty five years. One of the benefits of this longevity is the steady accumulation of information over a long period of time. It provides the feedstock for all of the historical valuations we are asked to perform for statutory purposes. Since our database extends back to 1971 (and earlier), we are able to conduct 1971 V-Day valuations for capital gains tax that can withstand the scrutiny of the Tax Court of Canada.

Take for instance the recent decisions in *Reiss Estate v. The Queen* which concerned the 1971 (V-Day) and 1990 (date of death) valuation of a large parcel of development land in Dartmouth. The Tax Court of Canada in its 1998 decision *(98 DTC 1455 T.C.C.)* had accepted much of our evidence on market value but did not fully adopt our final figures. On appeal, however, the Federal Court of Appeal whole-heartedly embraced our approach, preferring our reference data and methods to those of the Revenue Canada appraiser. With regard to the 1971 V-Day value, the only issue dealt with on appeal was the relevance of an earlier expropriation compensation award which we had introduced as cogent evidence of market value. The Tax Court judge had chosen to disregard it, but the Court of Appeal in its decision delivered in June 1999 agreed with our position that it was "relevant evidence" in establishing the market value of the land and should not have been ignored. The matter was then referred back to the Tax Court judge for reconsideration but was quickly settled to the taxpayer's benefit.

In our experience there is a growing tendency for accountants and lawyers to dispense with the V-Day reporting requirements as quickly and conveniently as possible, avoiding the expense of a proper valuation in favour of the published real estate assessment of the day. **It is a habit which almost always leaves tax dollars on the table.** The assessments of yesteryear often bore little if any relationship to the true market value of a property, more often than not **understating** the value by a large amount. It is significant that in the *Reiss Estate* case neither party made any attempt to rely on published assessments, and rightly so. The case was fought (and won) using conventional valuation methods which relied 100% on historical data.