

# 2016

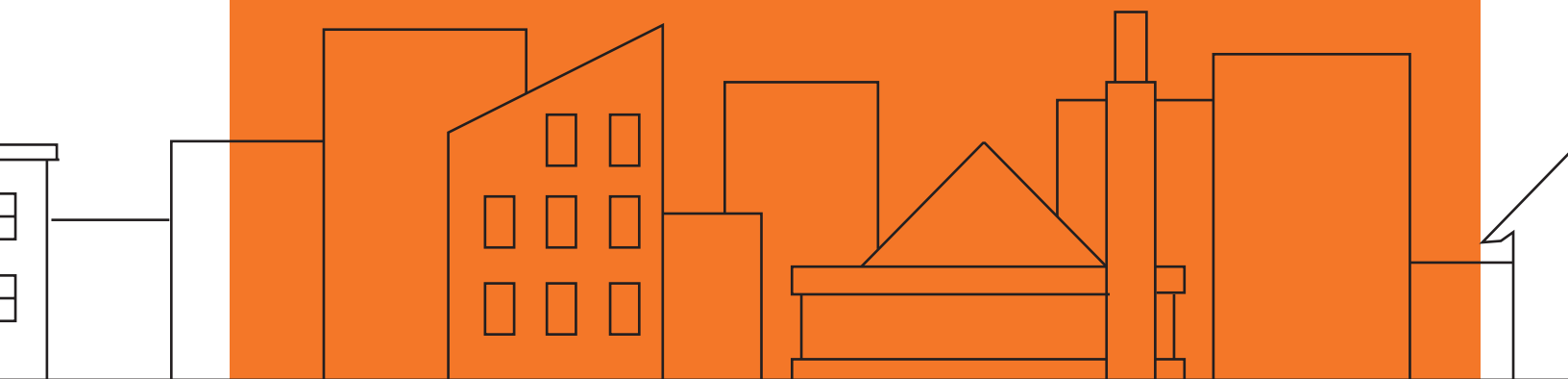
## ASSESSMENT METHODOLOGY

### HOTELS & MOTELS

A summary of the methods used by the City of Edmonton in determining the value of hotel and motel properties in Edmonton for assessment purposes.

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Edmonton




## Table of Contents

Scope.....	3
Introduction .....	3
Mass Appraisal .....	5
Valuation Model.....	6
Property Type.....	7
Approaches to Value.....	8
Income Approach (Hotel & Motel).....	8
Hotel Income Approach Definitions.....	9
Sample Pro forma .....	13
Ancillary Space Income Approach Definitions .....	14
Sample Ancillary Space Pro forma .....	17
Variables .....	18
Hotel/Motel Type.....	18
Location.....	18
Revenue .....	18
Expenses.....	18
Adjustments .....	18
Other Definitions .....	19
Provincial Quality Standards .....	19

## Scope

This guide is an aid in explaining how Hotel & Motel properties are valued for assessment purposes. The guide is intended as a tool; it is not intended to replace the assessor's judgment in the valuation process.

This icon  signifies when legislation is quoted.

## Introduction

Property assessments in the City of Edmonton are prepared in accordance with the requirements of the *Matters Relating to Assessment and Taxation Regulation*, Alta Reg 220/04, (hereinafter “MRAT”). This regulation establishes the valuation standard to be used, defines the procedures to be applied, and proposes objectives for the quality to be achieved in the preparation of assessments. The legislation requires the municipality to prepare assessments that represent *market value* by application of the *mass appraisal process*. All assessments are expected to meet quality standards prescribed by the province in the regulation.

Both *market value* and *property* are defined in the *Municipal Government Act*, RSA 2000, c M-26 (hereinafter the “MGA”):

*s. 1(1)(n) “market value” means the amount that a property, as defined in section 284(1)(r), might be expected to realize if it is sold on the open market by a willing seller to a willing buyer;*

In summary, commercial property assessments represent:

- an estimate of the value;
- of the fee simple estate in the property;
- as it existed on December 31, 2015;
- would have realized if it had been sold on July 1, 2015;
- on the open market and under typical market conditions;
- by a willing seller to a willing buyer.

The assessment is a prediction of the value that would result when those specific, defined conditions are met.

*“Fee simple interest [is] absolute ownership unencumbered by any other interest or estate...leased fee interest [is] the ownership interest held by the lessor, which includes the right to the contract rent specified in the lease plus the reversionary right when the lease expires....leasehold interest [is] the interest held by the lessee (the tenant or renter) through a lease conveying the rights of use and occupancy for a stated term under certain conditions.”*

Appraisal Institute of Canada, *The Appraisal of Real Estate Third Canadian Edition*, Vancouver, Canada, 2010, page 6.4.



s.284(1)(r) “**property**” means

- (i) a parcel of land
- (ii) an improvement, or
- (iii) a parcel of land and the improvements to it

MGA s.284(1)(r)

s.1(n) “**regulated property**” means

- (i) land in respect of which the valuation standard is agricultural use value,
- (ii) a railway,
- (iii) linear property, or
- (iv) machinery and equipment

MRAT s.1(1)(n)

s.6(1) the **valuation standard** for the land and improvements is market value unless subsection (2)... applies

MRAT s.6(1)

s.1(1)(n) “**market value**” means the amount that a property, as defined in section 284(1)(r), might be expected to realize if it is sold on the open market by a willing seller to a willing buyer

MGA s.1(1)(n)

s.2 An assessment of property based on **market value**

- (a) must be prepared using mass appraisal,
- (b) must be an estimate of the value of the fee simple estate in the property, and
- (c) must reflect typical market conditions for properties similar to that property

MRAT s.2

s.289(2) 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

MGA s.289(2)(a)

s.3 Any assessment prepared in accordance with the Act must be an estimate of the value of a property on **July 1** of the assessment year

MRAT s.3

s.1(k) “**mass appraisal**” means the process of preparing assessments for a group of properties using standard methods and common data and allowing for statistical testing

MRAT s.1(k)

## Mass Appraisal

Mass appraisal is the legislated methodology used by the City of Edmonton for valuing individual properties, and involves the following process:

- properties are stratified into groups of comparable property
- common property characteristics are identified for the properties in each group
- a uniform valuation model is created for each property group



27.1(c) **“valuation model”** means the representation of the relationship between property characteristics and their value in the real estate marketplace using a mass appraisal process

MRAT s.27.1(c)

The following two quotations indicate how the International Association of Assessing Officers distinguishes between mass appraisal and single-property appraisal:

*... “single-property appraisal is the valuation of a particular property as of a given date: mass appraisal is the valuation of many properties as of a given date, using standard procedures and statistical testing.”*

*... “Also, mass appraisal requires standardized procedures across many properties. Thus, valuation models developed for mass appraisal purposes must represent supply and demand patterns for groups of properties rather than a single property.”*

*The International Association of Assessing Officers, Property Appraisal and Assessment Administration, Chicago, Illinois, 1990, pg.88-89.*

For both mass appraisal and single-property appraisal, the process consists of the following stages:

	Mass Appraisal	Single Appraisal
Definition and Purpose	Mass appraisal is used to determine the assessment base for property taxation in accordance with legislative requirements	The client specifies the nature of the value to be estimated, including rights to be valued, effective date of valuation, and any limiting conditions
Data Collection	Mass appraisal requires a continuing program to maintain a current database of property characteristics and market information.	The extent of data collection is specific to each assignment and depends on the nature of the client's requirements
Market Analysis	Mass appraisal is predicated on highest and best use	Market analysis includes the analysis of highest and best use
Valuation Model	Valuation procedures are predicated on groups of comparable properties	Subject property is the focus of the valuation. The analysis of comparable properties is generally six or less
Validation	The testing of acceptable analysis and objective criteria	The reliability of the value estimate is more subjective. Acceptability can be judged by the depth of research and analysis of comparable sales

## Valuation Model

A valuation model creates an equation of variables, factors and coefficients that explains the relationship between estimated market value and property characteristics. An assessed value is then calculated by applying the appropriate valuation model to individual properties within a property type.



s.27.1(a) **“coefficient”** means a number that represents the quantified relationship of each variable to the assessed value of a property when derived through a mass appraisal process

(b) **“factor”** means a property characteristic that contributes to a value of a property;

(d) **“variable”** means a quantitative or qualitative representation of a property characteristic used in a valuation model

s.27.3(2) ...information that is required to be provided...does not include coefficients

*Province of Alberta. (2012). Matters Relating to Assessment and Taxation Regulation.*

### Valuation Model

- variables are created from property characteristics
- analysis of how variables effect market value
- factors and coefficients are determined
- the resulting valuation models are applied to property characteristics

## Property Type

### **Hotel/Motel**

Hotel & Motel properties provide rooms or suites for temporary accommodation which may include accessory food and beverage facilities, meeting rooms, and personal services shops. Hotel rooms have access from a common interior corridor while in motels each room or suite has its own exterior access.

**Resort hotels** are hotels with special recreational facilities to attract guests.

**Full Service hotels** provide a wide variety of facilities and amenities including food and beverage services owned and operated by the hotel, recreational facilities, and meeting rooms.

**Limited Service hotels** are properties with only some of the amenities found in full service properties. Limited Service Hotels often have food and beverage that is operated by a third party separately from the hotel's operations.

**Beverage hotels** are generally older facilities that have the majority of their business and income from beverage operations.

**Motels** are roadside hotels designed primarily for motorists. The rooms are typically arranged in a low rise building with exterior access, parking directly outside and generally cater to drive by traffic.

**Bed and Breakfast hotels** are typically a guest house or small hotel offering sleeping accommodations and a morning meal.

## Approaches to Value

The most common approaches to determine market value are the direct comparison, income, and cost. Each emphasizes a particular kind of market evidence.

### Direct Comparison Approach

Typical market value (or some other characteristic) is determined by referencing comparable sales and other market data and making appropriate adjustments. It is often used when sufficient sales or market data is available. It may also be referred to as the Sales Comparison Approach.

### Income Approach

This approach considers the typical actions of renters, buyers and sellers when purchasing income-producing properties. This approach estimates the typical market value of a property by determining the present value of the projected income stream. Often used to value rental or leased property.

### Cost Approach

Typical market value is calculated by adding the depreciated replacement cost of the improvements to the estimated value of land. It is often used for properties under construction or when there is limited market data available.

## Income Approach (Hotel & Motel)

In order to facilitate the valuation process, financial statements are annually received via the legislated Request for Information (RFI) process. Property owners are asked to provide four components including:

- A completed survey that asks for specific information about hotel operations such as occupancy percentages, average daily rates, FF&E expenditures, capital expenditures, etc.
- Complete financial statements with schedules of all expenses from the preceding three years
- Rent roll information that includes any leases that are held within the hotel property
- Franchise agreement, if applicable

Sales information is received from Land Titles. Sales are verified and validated by conducting site inspections and interviews, and by reviewing title transfers (change of ownership), sales validation questionnaires, and secondary data collection sources. The resulting verified and validated sales are used to develop capitalization rates to determine market value in the income approach. ***Sales reflect the condition of a property as of the sale date and thus may not always be equivalent to their assessed value.***

Sales occurring from July 1, 2010 to June 30, 2015 for valuation of Hotel & Motel properties were used.



## Hotel Income Approach Definitions

### Revenue

Revenue is separated into three categories: room, food & beverage, and other. The actual revenues from each hotel/motel property are stabilized over the three preceding years, in order to capture industry trends and minimize the impact when a hotel is not exhibiting normal operations within the hotel industry. This method is recommended by Municipal Affairs in the Hotel/Motel Valuation Guide. In general, stabilization involves weighing three years of revenue, with the greater weighting placed on more recent years, as follows:

70%	20%	10%
2014 revenue	2013 revenue	2012 revenue

If a property did not submit a usable financial statement for 2014, a typical adjustment was made to the 2013 revenue based on a typical year over year revenue change for that hotel type. A study was done to determine the typical year over year change of the revenue for each hotel type.

In cases where there is not three years of revenue information, the stabilization is adjusted. If only 2014 financial statements are available, the stabilized weight is 100%. If two years financials are available, it is stabilized at 70% for 2014 and 30% for 2013.

In addition, retail commercial space and parking revenue may be removed from the hotel revenue, where appropriate (e.g. a parkade open to the public), and will be captured in ancillary value in order to establish the final value.

**Room Revenue:** Room revenue is the revenue generated by the rental of the rooms.

**Food and Beverage Revenue:** Food and beverage revenue is the revenue generated by the food and beverage department.

**Other Revenue:** Any revenue that is not included in room revenue or food and beverage revenue. Examples of other revenue are storage, parking, movies, laundry, spa, snack bar and additional telephone and internet charges.

Below is a chart showing the types of revenue generated by each hotel/motel type:

Hotel Type	Room Revenue	Food & Beverage Revenue	Other Revenue
Resort	Yes	Yes	Yes
Full Service	Yes	Yes	Yes
Limited Service	Yes	No	Yes
Beverage	Yes	Yes	Yes
Motels	Yes	No	Yes
Bed & Breakfast	Yes	Yes	Yes

## Expenses

Allowable expenses are categorized into eleven different categories. Expense ratios for each expense category are determined for each hotel type.

**Allowable Expenses:** For assessment purposes, the following categories of expenses are used:

**Room Expenses:** are room staff (ie. Housekeeping) salaries, wages and benefits.

**Food & Beverage Expense:** are food & beverage costs and food department staff salaries, wages and benefits. This expense is only applicable to full service hotels and beverage hotels.

**Administration & General Expenses:** are salaries, wages and benefits of managers, human resource staff, accounting staff, night audit staff and security plus contract services, printing & stationery office supplies, uniform purchases, uniform cleaning, and vehicle expenses.

**Marketing & Promotions:** are any staff salaries, wages and benefits attributed to hotel advertising expenses.

**Repairs & Maintenance:** are expenses necessary to maintain the property, not including capital expenditures and items that are included in FF&E.

**Utilities:** are the costs of electricity, gas, water and sewage.

**Insurance:** are the costs associated with carrying commercial property insurance used to protect commercial property from such perils as fire, theft and natural disaster.

**Management Fee:** are the salaries and wages of the property managers.

**Franchise Fee:** are the costs associated with affiliating with a hotel franchisor. Only hotels that are affiliated with a franchise have this expense applied. Actual stabilized expenses are used for franchise fees, however, if a franchise hotel does not supply a franchise fee a typical is applied.

**Realty Taxes:** are expense levied against the property based on market value in order to pay for municipal services. The actual stabilized taxes are used and they are retrieved from the City of Edmonton database.

**Other Expenses:** are expenses that are the costs corresponding to other revenue. Stabilized actual expenses are used.

Allowable expenses are examined in two ways:

Expense Type	Typical Expense Ratio Used	Actual Expense Ratio Used
Room	X	
Food & Beverage	X	
Administration & General	X	
Marketing & Promotions	X	
Repairs & Maintenance	X	
Utilities	X	
Insurance	X	
Management Fees	X	
Franchise Fee		X
Taxes		X
Other Expenses		X

### Actual Expenses

For franchise fees, taxes, and other expenses the actual expenses incurred by each hotel over three years are applied using the 70%/20%/10% weighting.

70%	20%	10%
2014 expenses	2013 expenses	2012 expenses

### Typical Expenses

For the expense categories where typical expense ratios are used a typical expense ratio is established by stabilizing the expenses over three years using the same 70%/20%/10% stabilization formula.

Once the typical expense ratio is determined, the actual expense ratio will be compared to a range of + or – 10% of the typical expense ratio; this range is considered the industry norm. If actual expense ratios fall inside this range, then the actual expense ratio calculated for the building is used. If actual expense ratios fall outside of this +/- 10% range, then the industry norm is applied. When the actual expense ratio is lower than the -10% variance, then the low end of the industry norm range is used and when the actual expense ratio is higher than the +10% variance, then the high end of the industry norm range is used, as per the Practicing Assessment in Alberta Handbook – Hotel/Motel Valuation Guide – June 1998.

### Example:

	Typical	Actual	Factor used	Range		
				-10%	10%	
Rooms	30.0%	31.5%	31.5%	27.0%	33.0%	If ratio falls within -10%/+10% range, <b>Actual ratio</b> is used If ratio falls above +10% range, the <b>+10% maximum ratio</b> is used If ratio falls below -10% range, the <b>-10% minimum ratio</b> is used
Food & Beverage	45.0%	51.0%	49.5%	40.5%	49.5%	
Other Operated Departments	10.0%	8.5%	9.0%	9.0%	11.0%	

In cases where a financial statement has not been provided, is incomplete, or reported expenses deviate from normal or historical operations, an estimate of potential expenses is derived by examining the expenses of similar hotels. In cases where there is not three years of expense information, the stabilization is adjusted. If only 2014 financial statements are available, the stabilized weight is 100%. If two years financials are available, it is stabilized at 70% for 2014 and 30% for 2013.

**Non-allowable Expenses** are the following items:

- Fixtures and furniture (i.e. furniture, linens, towels, utensils, stoves and freezers) - Not included because they are related to the business enterprise.
- Capital expenditures – Not included because they provide additions or major improvements to the property that typically increase value and economic life.
- Debt Service/Mortgage interest payments – Interest and principle required to amortize a loan; it is a financing expense and not an operating expense.
- Income Tax – Not included because it is not an operating expense, it is a tax on personal income which may be affected by things other than the subject property.

- Depreciation – Not included because in the income approach it is recaptured in the capitalization rate rather than being included as an operating expense.
- Video Lottery and Gaming – Not included because they are related to the business enterprise.
- Expenses not required to maintain the property income – Not included because these are expenses not related to the property.

## Net Operating Income

Net operating income is the actual or anticipated (before income tax) net income from the operation of the property after deducting all expenses from the revenue. The term is often abbreviated to net income and sometimes stated as net income before recapture.

## Furniture, Fixtures and Equipment (FF&E)

This category is tangible non-realty assets or movable property of a business enterprise not classified as stock, inventory, or leasehold improvements. FF&E generally wears out much more rapidly than other components of a hotel or motel. This category contains guestroom, dining room, and lounge furnishings; kitchen equipment; front office and administrative equipment, decorative items, flooring, linens, glassware and china, etc. The City applies a consistent allowance to each hotel within each class (10% FF&E allowance for Limited, Motel, and Beverage; and 15% FF&E allowance for Full Service and Resort hotels).

## Intangibles and Business Component

This category represents the goodwill of the business, and is a percentage of the “Income before fixed charges” on the Assessment Proforma (1% allowance for Limited, Motel, and Beverage; and 1.5% allowance for Full Service and Resort hotels).

## Base Capitalization Rate

The capitalization rate is the rate reflecting the relationship between the assessable net operating income and the total price or value of the property. The cap rate converts the assessable net operating income into an indication of property value. The cap rate, in its basic formula, is found by dividing assessable net operating income by the sale price. Capitalization rate is applied based on hotel type and location.

The chart below summarizes the rates applied for capitalization rate, Intangibles & Business Component and Furniture, Fixtures & Equipment for each hotel type/location:

Hotel Type	Capitalization Rate	Intangibles & Business Component	Furniture Fixtures & Equipment
Resort	9.0%	1.5%	15%
Full Service - Downtown	9.0%	1.5%	15%
Full Service – Suburban	9.5%	1.5%	15%
Limited Service	9.5%	1.0%	10%
Beverage	9.5%	1.0%	10%
Motels	9.5%	1.0%	10%
Bed & Breakfast	10.0%	1.0%	10%

## Sample Pro forma

Hotel & Motel Valuation Summary					
Roll #:	999999999				Identifies Hotel/Motel Type and Property Information.
Address:	12345 - 678 Ave		Tax Year	2017	
Hotel Type:	Hotel Sample				
Rooms:	999				
Revenues		Total	Per Room	%	Actual Rooms, Food & Beverage, and Other Revenues stabilized over the three preceding years
Rooms		\$3,000,000	\$3,003	33.3%	
Food & Beverage		\$3,000,000	\$3,003	33.3%	
Other Operated Departments		\$3,000,000	\$3,003	33.3%	
<b>TOTAL REVENUES</b>		<b>\$9,000,000</b>	<b>\$9,009</b>	<b>100.0%</b>	
Departmental Expenses					
Rooms		\$750,000	\$751	25.0%	Stabilized Room Expense divided by Room Revenue
Food & Beverage		\$540,000	\$541	18.0%	Stabilized Food Expense divided by Food Revenue
Other Operated Departments		\$30,000	\$30	0.3%	Stabilized Other Expense divided by Total Revenues
<b>TOTAL DEPARTMENTAL EXPENSES</b>		<b>\$1,320,000</b>	<b>\$1,321</b>	<b>14.7%</b>	
<b>TOTAL DEPARTMENTAL INCOME</b>		<b>\$7,680,000</b>	<b>\$7,688</b>	<b>85.3%</b>	Stabilized Gen & Admin divided by Total Revenues
Undistributed Operating Expenses					
General & Administrative		\$1,737,000	\$1,739	19.3%	Stabilized Marketing & Promotion divided by Total Revenues
Marketing & Promotion		\$162,000	\$162	1.8%	
Repairs & Maintenance		\$324,000	\$324	3.6%	Stabilized Repairs & Maintenance divided by Total Revenues
Energy & Utility Costs		\$342,000	\$342	3.8%	Stabilized Energy & Utilities divided by Total Revenues
<b>TOTAL UNDISTRIBUTED OPERATING EXPENSES</b>		<b>\$2,565,000</b>	<b>\$2,568</b>	<b>28.5%</b>	
<b>INCOME BEFORE FIXED CHARGES</b>		<b>\$5,115,000</b>	<b>\$5,120</b>	<b>56.8%</b>	
Insurance					
Insurance on Buildings & Contents		\$45,000	\$45	0.5%	Stabilized Insurance divided by Total Revenues
<b>TOTAL INSURANCE</b>		<b>\$45,000</b>	<b>\$45</b>	<b>0.5%</b>	
<b>INCOME BEFORE OTHER FIXED CHARGES</b>		<b>\$5,070,000</b>	<b>\$5,075</b>	<b>56.3%</b>	
Management, Franchise Fees & Taxes					
Basic Management Fees		\$342,000	\$342	3.8%	Stabilized Basic Management Fee divided by Total Revenues
Franchise Fees		\$360,000	\$360	4.0%	Stabilized Actual Franchise Fee divided by Total Revenues
Taxes		\$140,099	\$140.24	9.4%	Stabilized Actual Property Taxes
<b>TOTAL MANAGEMENT, FRANCHISE FEES &amp; TAXES</b>		<b>\$842,099</b>	<b>\$843</b>	<b>9.4%</b>	
<b>NET OPERATING INCOME</b>		<b>\$4,227,901</b>	<b>\$4,232</b>	<b>47.0%</b>	
LESS INCOME ATTRIBUTABLE TO:					
% of Net Income Before Other Fixed Charges					
15%	FURNITURE, FIXTURES & EQUIPMENT	\$760,500	\$761		Ex: FF&E = Net Income Before Other Fixed Charges x 15%
1.5%	INTANGIBLES & BUSINESS COMPONENT	\$76,050	\$76		Ex: Intangibles = Net Income Before Other Fixed Charges x 1.5%
<b>ASSESSABLE NET OPERATING INCOME</b>		<b>\$3,391,351</b>	<b>\$3,395</b>		
7.5%	BASE CAPITALIZATION RATE				Market Value = NOI / Cap Rate Ex: \$3,391,351 / 7.5% = \$45,218,012
7.50%	<b>MRKT VAL OF HOTEL REAL ESTATE</b>	<b>\$45,218,012</b>	<b>\$45,263</b>		
	Ancillary Value	\$279,333			Refer to ANCILLARY page
Total Assessment for 2016 Tax Roll		\$45,497,346			
Total Assessment for 2016 Tax Roll (Rounded)		<b>\$45,497,000</b>			Final Market Value Estimate Utilizing the Income Approach

## Ancillary Space Income Approach Definitions

**Ancillary Space:** Ancillary space (not captured in the hotel proforma) is space that is leased to a third party, so it is valued separately from the hotel. The total value of this leased space is added to the hotel assessment to arrive at a final value for the entire hotel property.

- **Office** spaces are designed for general commercial occupancy, including administrative, government and corporate uses. Classification and location variables affect the rental rates applied to office spaces in hotels. See Office Methodology Guide for more information.
- **Retail** spaces are leased to facilitate commercial transactions. Classification, size, and location variables affect the rental rate applied to retail spaces in hotels. See Retail and Neighborhood, Power & Box Retail Methodology Guides for more information.
- **Warehouse** is space that is unfinished space that contains one or more bay doors. Classification, size, and location variables affect the rental rate applied to warehouse spaces in hotels. See Retail and Neighborhood, Power & Box Retail Methodology Guides for more information.
- **Parking** is typically charged a monthly rate per parking stall. See Retail Methodology Guides for more information. Parking type and location affect the rate applied to parking stalls for hotels. See Office Methodology Guide for more information.

**Typical Market Rent** is the rent currently prevailing in the market for properties comparable to the subject property (otherwise known as current economic rent). Current economic or market rents are used to form the basis of the valuation as opposed to actual rents, because in many cases actual rents reflect historical revenues derived from leases negotiated before the valuation date. In determining potential gross income, the assessor is not bound by the contractual rent between the landlord and tenant, but must determine rental income on the basis of what is typically paid in the market at the time of valuation.

**Base Rent / Net Rent** is the stipulated or contract rent exclusive of additional charges to the property (taxes, insurance, utilities and maintenance). Base and net rent do not include GST.

**Triple Net Rent** is the rental structure where the tenant (lessee) pays all charges to the property (e.g.: taxes, insurance, utilities, maintenance) in addition to the stipulated or contract rent. Structural repairs are excluded from the tenant responsibility.

**Effective Net Rent** is the rental term identifying the rental amount (usually in dollars per square foot of leased area) after adjustments have been made accounting for free rent periods, plus the present value of tenant improvement allowances and other inducements such as free parking.

**Lease types** include the terms gross lease, modified gross lease, single net lease, double net lease, and triple net lease. These may not always mean the same thing in different markets. The expenses that are included in each type of rent vary from market to market. In general, the following distinctions can be made:

- *Gross lease* - tenant pays rent and property owner pays expenses
  - *Modified gross lease (sometimes semi-gross)* - tenant and property owner share expenses
  - *Single net lease* - tenant pays utilities and taxes or insurance, and property owner pays structural repairs, property maintenance, and property taxes or insurance
-

- *Double net lease* - tenant pays utilities, taxes, and insurance, and property owner pays structural repairs and property maintenance
- *Triple net lease* - tenant pays utilities, taxes, insurance, and maintenance, and property owner pays for structural repairs only

**Operating Expenses (OE)** are the periodic expenditures necessary to maintain the real property and continue the production of the effective gross income; these are accounted for by the vacancy shortfall and structural allowances in the pro forma.

**Common Area Maintenance (CAM)** are the charges that reflect the costs of operating the interior and exterior common areas of a commercial property, and therefore include expenses for cleaning, utilities, heating, insurance, garbage & snow removal, and management fees.

**Potential Gross Income (PGI)** is the total current market rent for all space types that would be collected if the property were fully occupied at the date of valuation. In estimating PGI, the assessor distinguishes between market rent and contract rent. Market rent is the rate prevailing in the market for comparable properties and is used in calculating market value by the income approach. Contract rent is the actual amount agreed to by landlord and tenant.

***Potential gross income is derived by multiplying all Gross Leasable Areas (GLA) in the building by the current market rent for each particular space type.***



**Vacancy Allowance** is a deduction from the potential gross income for typical vacancy and collection losses, assuming current market conditions and typical management. Vacancy losses are best described as an allowance for vacant space. Collection losses are considered unpaid rents that the landlord is unlikely to recover. These allowances are usually expressed as a percentage of potential gross income. Variations in vacancy allowance can occur if vacancy greater than 10% is experienced for at least 3 consecutive years immediately preceding the valuation date. An allowance reflecting the stabilized chronic vacancy rate may be applied on a per building basis.

**Effective Gross Income (EGI)** is the anticipated income from all operations of real property adjusted for vacancy and collection loss.





**Net Operating Income (NOI)** is the actual or anticipated (before income tax) net income from the operation of the property after deducting all expenses from the effective gross income but before debt servicing costs. The term is often abbreviated to net income and sometimes stated as net income before recapture.

$$\text{EGI} - \text{OE} = \text{NOI}$$

**Structural Allowance** is an allowance provided to cover items which require periodic replacement because they wear out more rapidly than the building itself. Typically under the terms of conventional triple net leases, all operating expenses and property taxes are fully recouped by the landlord from the tenant. The only exception relates to items of a structural and/or capital nature, which are normally excluded from such recoveries. ***Rather than lump sum deductions, a structural allowance is applied annually over the economic life of the property regardless of whether any expenses were incurred in any given year.***

**Overall Capitalization Rate (Cap Rate)** is the rate reflecting the relationship between the anticipated net operating income from a single year (or an average of several years) and the total price or value of the property. The cap rate converts net operating income into an indication of property value. The cap rate, in its basic formula, is found by dividing net operating income by the sale price.

$$\text{NOI} \div \text{CAP RATE} = \text{MARKET VALUE ESTIMATE}$$



## Sample Ancillary Space Pro forma

PRO FORMA INCOME AND EXPENSE STATEMENT					
Roll #	999999999	Ancillary 1		Tax Roll Year	2017
PROJECTED GROSS INCOME				Assessor	
				Date	1-Jul-16
<b>MAIN FLOOR</b>		SIZE	RATE	TOTAL	
Office :			\$ -	\$ -	
Retail :		1125	\$ 20.00	\$ 22,500	
Warehouse :			\$ -	\$ -	
Parking :			\$ -	\$ -	
Other :			\$ -	\$ -	
GROSS INCOME MAIN FLOOR		1125		\$ 22,500	
LESS : Vacancy and Collection Loss			5%	\$ 1,125	
EFFECTIVE GROSS INCOME MAIN FLOOR				\$ 21,375	
<b>UPPER FLOORS</b>	# OF FLRS	SIZE	RATE	TOTAL	
Office :			\$ -	\$ -	
Retail :			\$ -	\$ -	
Warehouse :			\$ -	\$ -	
Parking :			\$ -	\$ -	
Other :			\$ -	\$ -	
GROSS INCOME UPPER FLOORS		0		\$ -	
LESS : Vacancy and Collection Loss			5%	\$ -	
EFFECTIVE GROSS INCOME UPPER FLOORS				\$ -	
<b>BASEMENT FLOORS</b>		SIZE	RATE	TOTAL	
Office :			\$ -	\$ -	
Retail :			\$ -	\$ -	
Warehouse :			\$ -	\$ -	
Parking :			\$ -	\$ -	
Other :			\$ -	\$ -	
GROSS INCOME OTHER FLOORS		0		\$ -	
LESS : Vacancy and Collection Loss			5%	\$ -	
EFFECTIVE GROSS INCOME OTHER FLOORS				\$ -	
<b>TOTAL EFFECTIVE GROSS INCOME</b>		1125		\$ 21,375	
LESS EXPENSES					
Structural Repairs			2%	\$ 428	
<b>ESTIMATED NET OPERATING INCOME</b>				\$ 20,948	
<b>CAPITALIZATION RATE</b>				7.5%	
<b>TOTAL VALUE</b>				\$ 279,300	
TOTAL VALUE per Total Sq Ft				\$ 248.27	
TOTAL VALUE per Above Grade Sq Ft				\$ 248.27	

**Ancillary PGI** = Ancillary GLA x Market Rent  
Ex: 1125 sq.ft x \$20.00 = \$22,500

**Vacancy Loss** = Ancillary PGI x Vacancy Rate  
Ex: \$22,500 x 5% = \$1125

**Effective Gross Income Main Floor Total** =  
Ancillary PGI less Vacancy  
Ex: \$22,500 - \$1125 = \$21,375

The total EGI for Main Floor, Upper Floor,  
and Basement Floors

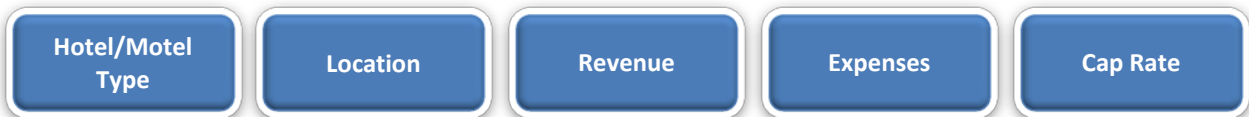
**Structural Repairs** = Structural Allowance  
x Total EGI  
Ex: \$21,375 x 2% = \$428

**Estimated Net Operating Income** = Total  
EGI less Structural Repairs  
Ex: \$21,375 - \$428 = \$20,948

**Market Value** = Estimated NOI / Hotel Cap  
Rate  
Ex: \$20,948 / 7.5 % = \$279,300

## Variables

Below is the list of variables that affect the assessment value for 2016.



### Hotel/Motel Type

See definitions under Property Type.

### Location

Full service hotels are the **only** hotel type that are stratified by location into either the Downtown area or Suburban. For hotels, the Downtown boundaries are 105 Avenue to the North, 95 Street to the East, the North Saskatchewan River to the South and 109 Street to the West. All other hotel types are assessed equitably within the specific hotel types.

### Revenue

See Revenue definitions above.

### Expenses

See Expense definitions above.

### Cap Rate

The capitalization rate applied to a hotel/motel varies based on type and location.

## Adjustments

**Additional Building** is the assessed value added for other buildings situated on the subject site.

**Associated Lots** is an adjustment based upon a separate but related parcel(s) required to satisfy the operation of another property.

**Buildings Under Construction** are improvements that are not complete as of the condition date. The adjustment is based on the cost rates from the Marshall & Swift manual, for the portion completed (also called percent complete).

**Construction Allowance (Shell Space Allowance)** is an allowance provided for leasable space that is without dividing walls, floor coverings, ceiling or other finishes. The adjustment is based on the cost rates from the Marshall & Swift manual.

**Excess Land** on an improved site is the land not needed to serve or support the existing improvement. It is also the portion of the parcel not needed to accommodate the site's primary highest and best use. Excess land may be separated from the larger parcel (sub-divided) and have its own highest and best use, or it may allow for future expansion of the existing or anticipated improvement. Excess land value is

derived from assessed commercial land values. Please refer to the 2016 Commercial Land Methodology Guide.

**Service Station Equipment (SSE)** is the improved value of the service station equipment, including pumps, underground tanks, canopy structures, car wash structures and equipment. The cost value is based on the Marshall & Swift Manual.

**Surplus Land** is the land not necessary to support the highest and best use of the existing improvement but, because of physical limitations, building placement, or neighbourhood norms, cannot be sold off separately. Surplus land may or may not contribute positively to value and may or may not accommodate future expansion of an existing or anticipated improvement.

## Other Definitions

**Actual zoning** is set by the Edmonton Zoning Bylaw 12800 and regulates the development of a parcel.

**Effective zoning** is applied to reflect the current use and development of a parcel. The effective zoning may differ the actual zoning when current use differs from that which is permitted by the actual zoning as updated by Edmonton Zoning Bylaw 12800 (ie. legal nonconforming use).

**Gross Building Area (GBA)** is the total floor area of a building, including below-grade space but excluding unenclosed areas, measured from the exterior of the walls. All enclosed floors of the building including basements, mechanical equipment floors, penthouses, and the like are included in the measurement. Parking spaces and parking garages are excluded.

**Gross Leasable Area (GLA)** is the total area designed for the occupancy and exclusive use of the tenants, including basements and mezzanines; measured from the centre of joint partitioning to the outside wall surface.

**Site Coverage** is the relationship, expressed as a ratio, between the total footprint area of the improvement(s) and the amount of land associated with it. Site coverage is used to determine if excess or surplus land exists.

## Provincial Quality Standards

The assessment models, the process utilized, and the results are submitted annually to the Assessment Services Branch of the Department of Municipal Affairs for audit purposes. This audit determines the accuracy of our predictions relative to the market place, and is a direct reflection on the accuracy of our models. The results indicated that the assessments meet Provincial Quality Standards as set out in *MRAT*.