

2019

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.

edmonton.ca/assessment

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Edmonton



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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 *Municipal Government Act*, RSA 2000, cM-26 (hereinafter "MGA") and the *Matters Relating to Assessment and Taxation Regulation*, 2018, Alta Reg 203/17, (hereinafter "MRAT"). The MRAT 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.

Commercial property assessments represent:

- an estimate of the value;
- of the fee simple estate in the property;
- as it existed on December 31, 2018;
- would have realized if it had been sold on July 1, 2018;
- 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.

Both *market value* and *property*, along with additional terms are defined in the MGA and MRAT :



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(k) "**regulated property**" means

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

MRAT s.1(k)

s.9(1) the **valuation standard** for the land and improvements is market value unless subsection (2)... applies

MRAT s.9(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.5 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.5

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.6 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.6

s.1(g) "**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(g)

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



31(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.31(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.”

Property Appraisal and Assessment Administration, 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.31(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*

MRAT, s.31 (a), (b) and (d)

s.33(3) Information prescribed...does not include coefficients

MRAT, s.33(3)

Valuation Model

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

Approaches to Value

The approaches to determine market value are the direct sales, income, and cost approaches.

Direct Sales Approach

Typical market value (or some other characteristic) is determined by referencing comparable sales and other market data. 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.

Sales Study

Sales information is received from Land Titles. Sales are validated. Validation may include; conducting site inspections and interviews, reviewing land title, title transfers (change of ownership), corporate searches, other land titles documents, sales validation questionnaires, and secondary data collection. The resulting validated sales are used to develop capitalization rates to use 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.***

For valuation of Hotel and Motel properties, sales occurring from **July 1, 2013** to **June 30, 2018** are used.

Request for Information (RFI)

In order to facilitate the valuation process, property owners are annually requested to provide three components via the legislated Request for Information (RFI) process, that comprises of:

- A completed **Hotel Motel Survey** that asks for specific information about the hotel's profile and operations such as Occupancy Rate, Average Daily Room Rates, FF&E and Capital Expenditures, Reserve for Replacement, and information pertaining to a major renovation.
- Most recent three years of accountant-prepared **Financial Statements** that includes the **Income Statements, Schedules of Income and Expenses** and **Notes**.
- A completed **Commercial Tenant Rent Roll** that ask for information of third-party leases that are held within the hotel property, as applicable.

Hotel Motel Valuation

Hotels are income producing properties that trade based on their income generating capabilities. For the purpose of assessment, these properties are valued on the Income Approach via Direct Capitalization Method. Below is the list of variables that affect the assessment value for 2019.

Hotel/Motel Stratification	Hotel Revenues	Hotel Expenses
Furniture, Fixtures & Equipment (FF&E)	Intangibles and Business	Capitalization Rate

Hotel Stratification

Hotels and Motels are designed and located to attract specific markets. Because hotel designs, facilities, amenities, and locations differ and directly impact financial operating results, it is important to define and accurately classify the different characteristics of lodging facilities (*Hotels Motels & Valuations and Market Studies, 2001, p. 155*).

Resort Hotels generally target family and leisure travelers. They may be adjacent or located near recreational facilities such as amusement theme parks, waterpark, golf courses, gaming & casino, ski slopes, or scenic areas. These type hotels are typically larger and offer a more exclusive, luxury chain.

Downtown Full-Service Hotels may range from luxury to mid-price and offer amenities such as restaurant, lounge, and conference & meeting rooms. They provide guest services such as concierge and room services. These hotels report Food and Beverage Departmental Revenues on their financial statements. These hotels are located within the boundaries of 105th Avenue to the North, 95th Street to the East, the North Saskatchewan River to the South and 109th Street to the West.

Suburban Full-Service Hotels may range from luxury to mid-price and offer amenities such as restaurant, lounge, and conference & meeting rooms. They often provide guest services such as concierge and room services. These hotels report Food and Beverage Departmental Revenues on their financial statements. These hotels are located outside of the Downtown boundaries of 105th Avenue to the North, 95th Street to the East, the North Saskatchewan River to the South and 109th Street to the West.

Limited Service Hotels have mainly room operations only. The hotel often have food and beverage that is operated by a third-party from the hotel's operations, and therefore do not report a Food and Beverage Departmental Revenues on their financial statements. These hotels are often economy-type hotels with very few other services and amenities offered by Full-Service hotels.

Beverage Hotels are generally facilities typically with less than 100 guest rooms. Majority of their business revenues are derived from the Food and Beverage operating department.

Motels are generally located along roadsides designed primarily for motorists. Typically, a low-rise building with exterior room access. Budget-type rooms that may range from daily room rates to extended stays of weekly or monthly room rates.

Hotel Revenue

Hotel Revenue is the sum of the amounts for all five categories of operating revenues with the exception of Limited and Motel stratified properties as these properties do not report a Food and Beverage Department on their financials.

Operating Revenues

Room Revenue: Primary source of revenue from the rental of rooms and suites to guest. Examples of the types of Room Revenue reported on financial statements include *Transient Rooms Revenue*, *Group Rooms Revenue*, *Contract Rooms Revenue*, and *Other Rooms Revenue* (such as weekly, bi-weekly, or monthly lodging).

Food and Beverage Revenue: Revenues of all sales of food and beverage from guests and patrons. Examples may be *Venue Food Revenue*, *In-Room Dining Food Revenue*, *Banquet / Conference/ Catering Food Revenue*, *Mini-Bar Food Revenue* and *Other Food Revenue*.

Other Operated Department Revenues: Other department(s) owned and operated by the hotel in generating revenue for profit and have direct operating expenses. Examples of Other Operated Department Revenue items would be *Guest Laundry Service*, *Business Center*, *Guest Shop*, *Front Shop* and *Valet & Lease Parking Revenues*.

Rent and Lease Revenue: Rental or concessions agreement between the hotel and retail tenant, offering hotel guest services and merchandises that are not provided by the operating department. Examples may be *Gift Shops*, *Restaurants*, *Retail Stores*, and *Valet & Lease Parking Revenues*.

Miscellaneous Revenue: Consist of sub-accounts or sub-schedules to provide more detail related to a particular income item. Items included in this category would be *Attrition Fees*, *Cancellation Fees*, *Cash Discounts Earned*, *Foreign Currency Gain*, and *Interest Income*.

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

Hotel Stratification	Room Revenue	Food & Beverage Revenue	Other, Rental and Misc. Revenue
Resort	Yes	Yes	Yes
Full Service - Downtown	Yes	Yes	Yes
Full Service - Suburban	Yes	Yes	Yes
Limited Service	Yes	No	Yes
Beverage Motels	Yes	Yes	Yes
Motel	Yes	No	Yes

Hotel Expenses

The expense of a hotel are typically allocated to one of three categories that reflects the nature of the expense: **Departmental Operating Expenses**, **Undistributed Operating Expenses**, and **Fixed Expenses**. These categories are then further categorized into a number of categories.

Departmental Operating Expenses

These expenses are related to an operating department revenue category.

Room Expenses: Room expenses consist of two major categories: Labour Cost and Related & Other Expenses. All payroll items associated with this department includes *Salaries, Wages, Service Charges, Contracted Labor, and Bonuses*. Room Related & Other Expenses include items such as *Room Cleaning Supplies, Commissions & Fees, Room Laundry, and Linen*.

Food & Beverage Expenses: Food & Beverage Expenses consist of two major categories: Cost of Food & Beverage Sales and Related & Other Expenses. Cost of Sales includes the cost of food served in all segments of food revenues. F & B Related and Other Expenses includes the cost associated with sale and service items such as *Labour Cost , Banquet Expenses, Flatware, Glassware, Linen, Kitchen Cleaning & Supplies, and Uniform*.

Other Departmental Expenses: Other Departmental Expenses are associated cost of sales and/or services to the corresponding Other Revenues. Items may include *Labour Cost, Cost of Goods Sold, and Valet & Lease Parking Expenses*.

Rent and Lease Expenses: Rent and Lease Expenses are associated cost of sales and/or services to the corresponding Rent and Lease Revenues. Items may include *Labour Cost, Cost of Goods Sold, and Rental Expenses*.

Miscellaneous Expenses: Miscellaneous Expenses are associated cost of sales and/or services to the corresponding Miscellaneous Revenues ledger. Items may include *Labour Cost, Cost of Goods Sold, Foreign Currency Exchange Loss, and Interest Expenses*.

Undistributed Operating Expenses

These expenses are considered applicable to the entire property. It is not appropriate to allocate these types of expenses to specific departments.

Administration & General: Admin & General expenses consists of two major categories: Salaries & Wages and Related Expenses. All payroll items associated with this department including *General Manager Salary, Employee Benefits and Bonuses*. Related Expenses includes items such as *Bank Interest and Charges, Credit Card Commission & Collection Fees, Donations, Dues and Subscriptions, Equipment Rental, Legal Services, Licenses and Permits, Professional Fees, Travel, Meals and Entertainments*.

Information and Telecommunication Systems: Items classified under this expense includes the hotel's centralized information system charges such as *accounting and security systems, point-of-sale reporting program, and internal reservation systems*. This category **does not include** transaction costs or commissions related to third party reservation or booking systems, or Telecommunications System for the hotel (i.e VoIP, T-1).

Sales & Marketing: Marketing expenses consist of two major categories: Salaries & Wages and Related Expenses. All payroll items associated with this department includes *Salaries, Wages, Employee Benefits, Bonuses and Contracted Work*. Related Expenses includes the associated cost of sales of goods and service items such as *Entertainments, Equipment Rental, Loyalty Programs, Operating Supplies, Promotion, Trade Shows, Training, Travel, Website, and Decorations*.

Property Operations and Maintenance: Maintenance expense consist of two major categories: Salaries & Wages and Related Expenses. All payroll items associated with this department includes *Salaries, Wages, Employee Benefits, Bonuses and Contracted Work*. Related Expenses may include maintenance expense items such as *Building, Electrical, Plumbing, Elevators, Kitchen & Laundry Equipment, Lights, Painting and Wallcovering, Swimming Pool, Vehicle Repair, Waste Removal, and Travel & Training*.

Utilities: Expense items attributing to this departmental expense would be *Electricity, Gas, Oil, Steam, Other Fuels, Contracted Services and Water/Sewer*. Cost expenses to this account would include the associated fee items such as *Taxes, Bulk/Future Purchase Fee, and Water Treatment/Filtration/Septic Tank* costs.

Management Fees: Management Fee is the contractual agreement cost between a third-party management company (Operator) and the hotel property owner (Investor). The Operator assumes complete responsibility for managing the hotel.

Franchise Fee: Franchise Fee is the contractual agreement cost between a hotel / motel company (a national or regional chain) and an independent hotel owner. The owner pays an annual negotiated fee (typically a percentage of the hotel's total annual gross revenues) to use the name, trademarks, and various services offered by the chain.

Fixed Expenses

Fixed expense by definition are costs that do not change with an increase or decrease in the amount of goods or services produced or sales volume.

Property Insurance: General insurance costs that includes premiums relating to liability and the property's business building and contents against damage or destruction by fire, weather, sprinkler leakage, terrorism, flood, boiler explosion, or plate glass breakage.

Property Tax: All taxes assessed against the real property by a government or public agency. City of Edmonton retrieves actual invoiced property tax amounts from the City's Assessment and Taxation system when ascribing the Property Tax expense amount on the subject hotel / motel's proforma.

Non-Allowable Expenses

These are expenses that often appear on financial statements but do not form part of property valuation.

- **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 and Amortization** – Not included because in the income approach it is recaptured in the capitalization.
- **Video Lottery and Gaming** – Current jurisprudence in Alberta, video lottery terminals and their incomes are not assessable for property taxes. However, the space occupied is assessable at its market value in the same way shopping centres apply the retail conditions for a kiosk.
- **Expenses not required to maintain the property income** – Certain expenses may not be included because these are expenses not related to the property. Examples of this include donations, litigation, bank charges, amortization, etc.

Stabilization

Reported actual revenues and expenses are stabilized over the three preceding years and the expenses are then normalized, as recommended by the *Province of Alberta - Municipal Affairs Hotel Motel Valuation Guide*, in order to capture industry performance and adjust for unforeseeable or atypical events that may significantly interrupt normal operations within the hotel.

Hotel and motels typically operates on short-term occupancies that range from a day to a week, and therefore the operating performance is sensitive to industry volatility and tends to fluctuate from year to year. The City of Edmonton stabilizes hotel/motel's revenue and operating expenses to derive a net operating income to be reflective of anticipated performance over its remaining economic life.

Stabilization accounts for the periodic life cycles of a hotel/motel such as growth, maturation, and declines. It may also mitigate or adjust for extraordinary events deemed temporary or non-recurring impacting revenues or expenses outside of hotel/motel's normal operations.

The City of Edmonton uses a **70-20-10** weighing of three years of revenue and expenses, with the greater weighting placed on the most recent **financial statements** prepared by an accountant prior to valuation date as of **July 1st, 2018**.

Example Scenario: A hotel's fiscal year-end is February 28th, 2018.

<p>70% Year-end Financial Statement dated February 28th, 2018</p>	<p>20% Year-end Financial Statement dated February 28th, 2017</p>	<p>10% Year-end Financial Statement dated February 28th, 2016</p>
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If a property did not submit complete or usable financial statements at the time of the Request for Information period, a projected revenue adjustment is ascribed based on the City of Edmonton's **Occupancy** and **Average Daily Room Rate** study from returned RFI's of similar stratified hotel and motels. In other cases, where a hotel or motel is recently constructed, or insufficient financial information is available, the assessor may utilize the cost approach to determine a valuation. For more information on the cost approach to valuation, please see the City's 2019 Cost Approach Methodology Guide.

Industry Norms

Once expenses have been collected from property owners through the RFI process, the appropriate data is analyzed according to operating expense categories to derive the **Industry Norms** (or **Typical Expenses Ratios**), so that consistent valuation parameters and other statistical measures can be developed across each hotel stratification type. An expense ratio is calculated by dividing the stabilized expense by the associated revenue.

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 ascribing the industry norms of similar stratified hotels/motels.

Normalization

Once the Industry Norm percentages are established, the actual expenses will be compared to the **+/- 10%** range from the industry norm percentage; this process is called **Normalization**. 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 the **+/- 10%** range, then the industry norm is applied. For example, 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.

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

Application of Normalization for Allowable Expenses

Below is a chart that indicates whether a typical or actual expense ratio is applied for each expense category:

Expense Type	Typical Expense Ratio Used	Actual Expense Ratio Used
Room	X	
Food & Beverage	X	
Other, Rental, Misc.		X
Administration & General	X	
Information & Telecommunication System		X
Sales & Marketing	X	
Property Operations & Maintenance	X	
Utilities	X	
Management Fees	X	
Franchise Fees		X
Property Insurance	X	
Property Taxes		X

Furniture, Fixtures and Equipment (FF&E)

FF&E are 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 Guest Room, Dining Room and Lounge furnishings; Kitchen Equipment, Front Office and Administrative Equipment, Decorative Items, Flooring, Linens, Glassware, and China.

The City applies a consistent allowance within each stratification: **15%** FF&E Allowance for Full Service and Resort hotels; **10%** FF&E Allowance for Limited Hotels, Beverage Hotels and Motels.

Intangibles and Business Component

This category represents the goodwill of the business, and is a percentage of the '*Net Operating Income Before Fixed Charges*' on the Assessment Proforma: **1.5%** allowance for Full Service and Resort hotels; **1.0%** allowance for Limited Hotels, Beverage Hotels and Motels.

Capitalization Rate

The Capitalization Rate is the rate reflecting the relationship between the Assessable Net Operating Income and the Market Value to Real Estate 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 Stratification.

The chart below summarizes the rates applied for **Capitalization Rate, Intangibles & Business Component, and Furniture, Fixtures, & Equipment** for each Stratification. These rates are derived from sales of comparable properties and the information provided from property owners through the RFI process.

Stratification	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	10.0%	1.0%	10%
Motels	10.0%	1.0%	10%

Sample Assessment Pro Forma

Building: City of Edmonton Hotels and Motels	Actual Zoning: CHY	Identifies Hotel/Motel Stratification and Property Profile.
Roll #: 123456789	Effective Zoning: CHY	Hotel/Motel's Actual & Effective Zoning
Address: 123456	Assessment Year: 2019	
Stratification: Downtown Full-Service		
Rooms: 123		

Operating Revenues	Total	Per Room	%
Rooms	\$4,600,000	\$37,398.37	51.6%
Food & Beverage	\$3,600,000	\$29,288.29	40.4%
Other Operated Departments	\$660,000	\$5,365.85	7.4%
Rental Income	\$52,000	\$423	0.6%
Miscellaneous	\$8,400	\$68	0.1%
Total Operating Revenues	\$8,920,400	\$72,524	100.0%

Actual Operating Revenues stabilized over the three preceding years.

Total Operating Revenues = Room Revenues + Food & Beverage Revenues + Other Operated Department Revenues + Rental Revenue + Miscellaneous Revenues

Departmental Operating Expenses	Total	Per Room	%
Rooms	\$1,472,000	\$11,967.48	32.0%
Food & Beverage	\$2,448,000	\$19,902.44	68.0%
Other Operated Departments	\$44,602	\$362.62	0.5%
Rental Expenses	\$89,204	\$725	1.0%
Miscellaneous	\$17,841	\$145	0.2%
Total Departmental Expenses	\$4,071,647	\$33,103	45.6%
Net Departmental Income	\$4,848,753	\$39,421	54.4%

Stabilized Room Expenses divided by Room Revenue.

Stabilized Food & Beverage Expense divided by Food & Beverage Revenue.

Stabilized Other Operated Departments divided by Total Operating Revenues.

Stabilized Rental divided by Total Operating Revenues.

Stabilized Miscellaneous divided by Total Operating Revenues.

Total Operating Expenses = Rooms Expense + Food & Beverage Expense + Other Operated

Total Departmental Income = Total Operating Revenues - Total Departmental Expenses

Undistributed Operating Expenses	Total	Per Room	%
Administrative & General	\$802,836	\$6,527.12	9.0%
Information & Telecommunications Systems	\$44,602	\$363	0.5%
Sales & Marketing	\$356,816	\$2,900.94	4.0%
Property Operation & Maintenance	\$490,622	\$3,988.80	5.5%
Utilities	\$383,577	\$3,118.51	4.3%
Management Fee	\$356,816	\$2,900.94	4.0%
Franchise Fee	\$356,816	\$2,901	4.0%
Total Undistributed Operating Expenses	\$2,792,085	\$22,700	31.3%
Net Operating Income Before Fixed Charges	\$2,056,668	\$16,721	23.1%

Stabilized Administration & General divided by Total Operating Revenues.

Stabilized Information and Telecommunication Systems divided by Total Operating Revenues.

Stabilized Sales & Marketing divided by Total Operating Revenues.

Stabilized Property Operation and Maintenance divided by Total Operating Revenues.

Stabilized Utilities divided by Total Operating Revenues.

Stabilized Management Fee divided by Total Operating Revenues.

Stabilized Franchise Fee divided by Total Operating Revenues.

Total Undistributed Operating Expenses = Administrative & General + Information and Telecommunications System + Sales & Marketing + Property Operation and Maintenance + Utilities + Management Fee + Franchise Fee

Total Departmental Income = Total Operating Revenues - Total Departmental Expenses

Fixed Expenses	Total	Per Room	%
Property Insurance	\$44,602	\$363	0.5%
Property Tax	\$338,975	\$2,756	3.8%
Total Fixed Expenses	\$383,577	\$3,119	4.3%
Net Operating Income	\$1,673,091	\$13,602	18.8%

Stabilized actual Property Insurance divided by Total Operating Revenues.

Stabilized actual Property Taxes divided by Total Operating Revenues.

Total Fixed Expenses = Property Insurance + Property Taxes

Net Operating Income = Net Operating Income Before Fixed Charges - Total Fixed Expenses

<i>Less % of NOI before Fixed Charges: Furniture, Fixtures, & Equipment</i>	\$308,500	\$2,508	15.0%
<i>Less % of NOI before Fixed Charges: Intangibles & Business Component</i>	\$30,850	\$251	1.5%
Assessable Income to Real Estate	\$1,333,741	\$10,843	

FF&E = Net Income Before Fixed Charges x 15.0%

Intangibles & Business Components = Net Income Before Fixed Charges x 1.5%

Assessable Income to Real Estate = Net Operating Income - FF&E - Intangible & Business Component

Capitalization Rate	9.00%	
Market Value to Real Estate	\$14,819,340	
Ancillary Value	\$4,189,500	

Market Value = NOI divided by Capitalization Rate

Refer to ANCILLARY page

Total Assessment for 2019 Tax Roll	\$19,008,840	
Total Assessment for 2019 Tax Roll (Rounded)	\$19,008,500	\$154,540.65

Total Assessment for 2017 Roll = Market Value to Real Estate + Ancillary Value + Parkade

FINAL MARKET VALUE

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Ancillary Space Income Approach Variables

Ancillary Space: Ancillary space(s), not captured in the hotel pro forma, 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. Location of the hotel affects the rental rates applied to office spaces in hotels. Please refer to *2019 Assessment Methodology - Downtown/Suburban Office* for location definitions. Rental rates for office spaces will be derived in accordance with the *Retail and Retail Plaza* methodology guide. The capitalization rate applied to the office spaces will be consistent with that applied to the entirety of the hotel property.
- **Retail** spaces are leased to facilitate commercial transactions. Size, and location of the hotel affect the rental rate applied to retail spaces in hotels. Please refer to *2019 Assessment Methodology - Retail and Retail Plaza* for size and location definitions. Rental rates for retail spaces will be derived in accordance with the *Retail and Retail Plaza* methodology guide. The capitalization rate applied to the retail spaces will be consistent with that applied to the entirety of the hotel property.

Other Ancillary Space Income Approach Definitions

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 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 *gross leases, modified gross leases, single net leases, double net leases, and triple net leases*. 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 or structural repairs only
 - **New** is a new lease agreement of a tenant occupying a space that was vacant or occupied by a previous tenant, may include tenant expansion.
 - **Renewal** is when a lease expires and the existing tenant signs a new lease term.
 - **Step-Up** is a scheduled change to the rental rate within the term of the existing lease.

Tenant Improvement Allowances is a dollar amount or allowance provided to the tenant by the landlord for the renovation or completion of the interior finish, which may or may not equal the full cost of construction or remodelling.

The City of Edmonton does not adjust for tenant improvement allowances. As the City is mandated through legislation to assess the *Fee Simple interest* of each property, it is inherent that the estimated market rent reflect fully finished space. When a tenant and landlord negotiate a base rental rate with a tenant improvement allowance as part of the rental agreement, they have agreed upon the rent that they believe the space can achieve as fully finished, not the rent it would achieve in its current state.

Tenant Inducements are incentives provided by landlords either to attract new tenants or retain existing tenants. Described below are the most common forms of tenant inducements:

- *Common area expense or operating expense reimbursement* is a form of tenant inducement where operating expenses in excess of a predetermined base amount are reimbursed.
- *Relocation Allowance* is a credit offered by a landlord to cover relocation expenses incurred by tenants.
- A *buyout* is a termination of an existing lease whereby the landlord agrees to pay the remainder or terminate the original lease on behalf of the tenant.
- *Cash payments* are a signing bonus paid to tenants that enter into a new lease agreement.
- *Free rent or discounted rent* is an abatement of rent during some period of the lease term. Free rent is a reduction in the face rental rate, the amount appearing on the face of the lease, for a stated period of time. This adjustment is generally applied at the beginning of the lease term. For example, a lease is signed with free rent for the first three months of a five year lease.

Based on the information provided to the City of Edmonton through the RFI process, for 2019 valuation,

there were no types of tenant inducements that were found to be typical in the marketplace for Hotel Motel ancillary spaces. Therefore, no adjustments were applied when determining typical market rent.

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.

$$\text{GLA} \times \text{Market Rent for Space} = \text{PGI}$$

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 (such as chronic vacancy) can occur if vacancy greater than 10% is experienced for at least 3 consecutive years immediately preceding the valuation date.

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

$$\text{PGI} - \text{Vacancy Allowance} = \text{EGI}$$

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 Proforma

Ancillary Proforma

Roll #: 123456789
Address: 123456
Tax Year: 2019

Main Floor	Business Name	Leased Size (sq.ft)	Rate (\$ / sq.ft)
Office			\$ -
Retail	ABC Ltd.	10000	\$ 30.00
Warehouse			\$ -
Parking			\$ -
Other			\$ -
Total		10000	

Total Net Income Main Floor
Less: Vacancy and Collection Loss 5.00%
Net Income Main Floor

Total
\$0
\$300,000
\$0
\$0
\$0
\$0
\$300,000

Ancillary NOI = Ancillary GLA x Market Rent
Ex: 10,000 sq.ft x \$30.00 = \$300,000

\$300,000
\$15,000
\$285,000

Vacancy Loss = Ancillary NOI x Vacancy Rate
Ex: \$300,000 x 5.00% = \$15,000

Upper Floor(s)	Business Name	Leased Size (sq.ft)	Rate (\$ / sq.ft)
Office	ABC Ltd.	4000	\$ 25.00
Retail			\$ -
Warehouse			\$ -
Parking			\$ -
Other			\$ -
Total		4000	

Net Income Upper Floor(s)
Less: Vacancy and Collection Loss 5.00%
Net Income Upper Floor(s)

Total
\$100,000
\$0
\$0
\$0
\$0
\$0
\$100,000

Effective Gross Income = Ancillary NOI - Vacancy Loss
Ex: \$300,000 - \$15,000 = \$285,000

\$100,000
\$5,000
\$95,000

Basement Floor	Business Name	Leased Size (sq.ft)	Rate (\$ / sq.ft)
Office			\$ -
Retail			\$ -
Warehouse			\$ -
Parking			\$ -
Other	ABC Ltd.	500	\$ 10.00
Total		500	

Net Income Basement Floor
Less: Vacancy and Collection Loss 5.00%
Net Income Basement Floor

Total
\$0
\$0
\$0
\$0
\$0
\$5,000
\$5,000

Total Net Income for Main Floor, Upper Floor, and Basement Floor.

\$5,000
\$250
\$4,750

Structural Allowance = Total Net Income x Structural Allowance %

Total Net Income
Less: Structural Allowance 2.00%

\$384,750
\$7,695

Net Operating Income

\$377,055

Capitalization Rate 9.0%

Hotel's Capitalization Rate

Ancillary Value **\$4,189,500**

Estimated Ancillary Market Value



Other Value Adjustments

Additional Building is the assessed value added for other buildings situated on the subject site. The method of valuation of an additional building will depend on the nature and function of the building.

Associated Lots is a reduction to a primary improved property based upon a separate but related associated parcel(s). This adjustment is applied when all, or part, of the land from the associated parcel(s) is required to satisfy the operation of the primary property. The associated parcel(s) must be owned by the same individual/corporation as the primary improved property or have a lease in place with the primary improved property. The *Edmonton Zoning Bylaw No.12800* outlines the requirements to satisfy the operations of the primary 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).

Excess Land on an improved parcel 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 parcel's primary highest and best use. Excess land may be separated from the larger parcel (subdivided) 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 *2019 Commercial Land Assessment Methodology*.

Edmonton Zoning Bylaw No.12800 is used to determine the appropriate parking requirements for calculating the amount of excess land in the Office inventory.

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 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 non-conforming 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.

Revision History

February 21, 2019 - removed Provincial Quality Standards section

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