MUNICIPAL
PROPERTY
ASSESSMENT
CORPORATION

# METHODOLOGY GUIDE

## VALUING MOTELS IN ONTARIO

**Valuation Date: January 1, 2016**

AUGUST 2016

MUNICIPAL PROPERTY ASSESSMENT CORPORATION

August 22, 2016

The Municipal Property Assessment Corporation (MPAC) is responsible for accurately assessing and classifying property in Ontario for the purposes of municipal and education taxes.

In Ontario's assessment system, MPAC assesses your property value every four years. This year, MPAC is updating the value of every property in the province to reflect the legislated valuation date of January 1, 2016.

MPAC is committed to provide Ontario property owners, municipalities and all its stakeholders with the best possible service through transparency, predictability and accuracy in values. As part of this commitment, MPAC has defined three levels of disclosure of information in support of its delivery of this year's assessment update. This Methodology Guide is the first level of information disclosure.

This guide provides an overview of the valuation methodology undertaken by MPAC when assessing motel properties for this year's update ensuring the methodology for valuing these properties is well documented and in alignment with industry standards.

Property owners can access additional information about their own properties through aboutmyproperty.ca. Login information for aboutmyproperty.ca is provided on each Property Assessment Notice mailed this year. Additional information about MPAC can be accessed at mpac.ca.

Antoni Wisniowski

President and Chief Administrative Officer

Rose McLean, M.I.M.A.

Chief Operating Officer

## Table of Contents

## 1.0 Introduction

The Municipal Property Assessment Corporation (MPAC) – mpac.ca – is responsible for accurately assessing and classifying property in Ontario for the purposes of municipal and education taxation.

In Ontario, property assessments are updated on the basis of a four-year assessment cycle. In 2016, MPAC will update the assessments of Ontario's nearly five million properties to reflect the legislated valuation date of January 1, 2016. Assessments updated for the 2016 base year are in effect for the 2017–2020 property tax years.

The last Assessment Update was based on a January 1, 2012, valuation date. Increases between the 2012 assessed value and the 2016 assessed value are phased in over a four-year period. Any decreases in assessment are applied immediately.

It is important to ensure that the valuation methodology applied is capable of providing a realistic estimate of current value at the relevant valuation date, which, in turn, enables all stakeholders to understand the valuation process and have confidence in the fairness and consistency of its outcome.

This Methodology Guide has been prepared for the benefit of MPAC assessors, property owners and their representatives, municipalities and their representatives, Assessment Review Board members, provincial officials, and the general public.

This guide outlines the valuation process to be followed by an assessor, including steps that require appraisal judgment. It is incumbent upon the assessor to make informed decisions throughout the valuation process when arriving at estimates in current value.

### 1.1 Properties Covered by This Methodology Guide

Motel properties vary considerably. They may provide short- or long-term lodging. Motels are usually located with good access to major road networks and situated near highways or on the outskirts of major or small cities/towns. They typically have fewer amenities than hotels.

Motel structures are generally single- or two-storey buildings with connected rooms. Many have open walkways and exterior entrances.

The following MPAC property codes are used to categorize motels in Ontario:

- 450 Motel

 

- 451 Seasonal Motel

It should be noted that these are general guidelines that vary depending on the specific circumstances of a particular property.

An assessor may also make reference to additional Methodology Guides for properties that do not fall precisely within the description of one of the property codes listed above.

## 1.2 Legislation

The main legislation governing the assessment of properties in Ontario for property tax purposes is contained in the Assessment Act.[1]

The Act contains important definitions and states that all property in Ontario is liable to assessment and taxation, subject to some exemptions. Section 19(1) of the Act requires that land be assessed at current value, which is defined to mean, in relation to land, “the amount of money the fee simple, if unencumbered, would realize if sold at arm’s length by a willing seller to a willing buyer.”

The Minister of Finance filed Ontario Regulation 430/15 on December 18, 2015, which added additional rules affecting the valuation and classification of properties on which a third-party sign (billboard) is located. To comply with the regulation, the income attributable to a third-party sign will not be included in the valuation of any property for assessment purposes.

## 1.3 Classification

MPAC’s role is to accurately assess and classify all properties in Ontario in accordance with the Assessment Act and its associated regulations established by the Government of Ontario. The classification of a property will determine which tax rate will be applied by the municipality or taxing authority. All properties are classified according to their use, and Ontario Regulation 282/98 of the Assessment Act sets out how various property uses are classified.

Motels are included in the commercial property class in accordance with Section 5(1)1 of Ontario Regulation 282/98 as “land and vacant land that is not included in any other property class.”[2]

Most motels also contain residential living quarters that are typically occupied by the owner/operator. These areas are classified in the Residential Property Class in accordance with Section 3(1)1 of Ontario Regulation 282/98.

---

[1] Assessment Act, R.S.O 1990, c A.31: https://www.ontario.ca/laws/statute/90a31.
[2] Ontario Regulation 282/98, GENERAL: https://www.ontario.ca/laws/regulation/980282.

 

If a portion of the property is used for other purposes, the total value of the property will be apportioned between the various uses to ensure that the appropriate tax rate is applied to the relevant parts of the property.

### 1.4 The Use of This Methodology Guide

This Methodology Guide is intended to:

- Ensure MPAC's assessed values for these properties are fair, accurate, predictable, and transparent.

- Provide direction to assessors and clear explanations to municipalities, taxpayers, and Assessment Review Board members.

- Ensure that MPAC's methodology for valuing these properties is well documented and aligns with industry standards.

- Explain the thought process/decision-making process that an assessor should undertake to apply the valuation methodology.

- Ensure a consistent approach to valuing these property types.

- Support MPAC assessors in conducting their due diligence in:

    - applying Ontario's legislation and regulations
    - adhering to industry standards for market valuation in a mass appraisal environment

It should be noted that this Methodology Guide is not intended to be a substitute for an assessor's judgment in arriving at a market value–based assessment (i.e., current value) for a particular property. However, given that the Methodology Guide explains industry standards for property assessment, conforms to valuation industry norms, and adheres to provincial legislation and regulation, MPAC assessors are expected to follow the procedures in the Methodology Guide and be able to clearly and satisfactorily justify any deviations from it.

### 1.5 Consultation and Disclosure

MPAC is committed to providing municipalities, taxpayers and all its stakeholders with the best possible service through transparency, predictability and accuracy. In support of this commitment, MPAC has defined three levels of disclosure as part of its delivery of the 2016 province-wide Assessment Update:

 

- **Level 1** – Methodology Guides explaining how MPAC approached the valuation of particular types of property
- **Level 2** – Market Valuation Reports explaining how the methodology outlined in Level 1 has been applied at the sector level for the purposes of each assessment
- **Level 3** – Property Specific Valuation Information available to property taxpayers, their representatives and municipalities

Residential property owners can access detailed information about their assessment through aboutmyproperty.ca. Login information is provided on every 2016 Property Assessment Notice mailed.

 

## 2.0 The Valuation Process

The valuation process always begins with a determination of the highest and best use of the subject property.

Any reliance upon this guide is made only after the assessor has determined that the highest and best use of the subject property is that of a motel.

Assessors determine the value of a property using one of three different approaches to value:

- the direct (sales) comparison approach
- the income approach
- the cost approach

### 2.1 Outline

In the **direct (sales) comparison approach**, value is indicated by recent sales of comparable properties in the market. In considering any sales evidence, it is critical to ensure that the property sold has a similar or identical highest and best use as the property to be valued.

In the **income approach** (or, more accurately, the income capitalization approach), value is indicated by a property's revenue-earning power, based on the capitalization of income. This method requires a detailed analysis of both income and expenditure, both for the property being valued and other similar properties that may have been sold, in order to ascertain the anticipated revenue and expenses, along with the relevant capitalization rate.

Motel valuation employs a simplified version of the income approach as a GIM (gross income multiplier) is used to establish the relationship between gross income and value. The GIM is derived from a detailed analysis for similar properties that have been sold.

In the **cost approach**, value is estimated as the current cost of reproducing or replacing the improvements of the land (including buildings, structures and other taxable components), less any loss in value resulting from depreciation. The market value of the land is then added.

MPAC uses the income approach to value motels. For this type of property, the gross income multiplier (GIM) method of the income approach is used. The following steps are followed:

1) Collect income, expense and other appropriate information from motel management and other sources.

2) Analyze the data and establish industry norms – gross income, occupancy, expense ratios, etc., for motels accounting for size, age, quality and location.

3) Analyze income and expense data, and stabilize data to reflect typical three-year performance.

4) Compare actual income and expenses with similar motels in each locality in Ontario.

5) Establish gross income multipliers (GIM) from the sales data.

6) Calculate the motel value by multiplying the stabilized gross annual income by the GIM.

7) Deduct personal property allowance.

8) Calculate the current value of real estate by subtracting the personal property allowance from the motel value.

9) Add value of other components located on the property (residential living quarters, excess lands) to produce the current value of the property.

10) Review the outcome to verify accuracy.

## 2.2 Approach

There are three main phases in the process used by MPAC:

- data collection
- analysis of the data collected
- valuation

## 2.3 Data Collection

Application of the GIM requires the collection of financial and general data, including:

*General Motel Data*

- inspecting, measuring and quantifying motel improvements
- identifying improvement ages and functions
- collecting data for numbers of rooms and amenities, car parking, etc.
- obtaining building and site improvement plans for the subject property

 

*Motel Financial Data*

- collecting income and expense statements relating to the motel for at least three years
- examining income and expense statements to confirm that they are typical and reflective of the marketplace
- tabulating motel revenues  and other income valuation parameters

**Information from Owners**

The owner or operator is the main source of financial data relating to the motel. Although the data requested by MPAC may vary depending upon the type of motel concerned and the amenities provided, it may include the following:

- occupancy levels
- average room rate
- other income (mini-bar, catering, conference room rentals, movies, etc.)
- operating expenses for the motel
- other operating expenses broken down by type of expense
- management contract details
- record of expenditures on FF&E
- record of capital expenditures

MPAC also requests data on motel sales. The data requested relates to the sale price, gross income and other relevant information helpful in identifying which sales are open market transactions, the circumstances of each transaction and the motivation of the parties.

Each sale is investigated and where all relevant information is collected, a GIM is calculated. Sales data is compiled and an analysis is conducted to determine GIM ranges for properties based on size, age, type, location and quality. These GIMs can then be applied to similar properties that have not sold.

Sales where GIMs cannot be calculated are not included in the GIM study but are not discarded as they may still offer some valuable metrics such as sale price per room.

 

**Confidentiality**

As outlined above, it is important to be aware that, in order to enable MPAC to produce an accurate valuation of the property concerned, information needs to be obtained from a variety of sources.

This will include information from MPAC's records, from the owner or operator of the property, from the municipality in which the property is located, from the assessor's visit to the property, and from other sources.

All stakeholders in the property tax system have an interest in ensuring that the current value provided by MPAC is correct; in order to achieve this, it is necessary for all parties to cooperate in the provision of information.

It is appreciated that some of the information outlined above may be of a commercially sensitive nature. MPAC recognizes the need to ensure that any information provided to it is properly safeguarded and only used for the purpose for which it is supplied. Assessors must appreciate the nature of this undertaking and ensure data is treated accordingly.

If, after an appeal has been filed, MPAC receives a request for the release of actual income and expense information, or other sensitive commercial proprietary information, the usual practice is to require the person seeking the information to bring a motion before the Assessment Review Board (ARB), with notice to the third parties, requesting that the ARB order production of the requested information. The release of such information is at the discretion of the ARB and commonly accompanied by a requirement for confidentiality.

The Assessment Act outlines in Section 53(2) that disclosed information may be released in limited circumstances "(a) to the assessment corporation or any authorized employee of the corporation; or (b) by any person being examined as a witness in an assessment appeal or in a proceeding in court involving an assessment matter."

### 2.4 Data Analysis

The analysis process involves several steps:

1) The first task is to *qualify* the data before it is used to establish the rates and factors that will be used to value the properties.

2) Next, the data is *classified* so that it can be sorted into appropriate groups, which reflect conditions where data comparisons can be made and conclusions drawn.

3) Finally, the specific individual valuation parameters are developed.

 

### 2.5 Valuation

Having undertaken the necessary steps outlined above, the assessor should now be in a position to apply the appropriate valuation model.

### 2.6 Validating the Results

Once the assessor has completed the valuation, it is necessary to carry out a series of checks to ensure that all relevant parts of the property have been included in the valuation, there has been no double-counting of any adjustments made for depreciation, the resulting valuation has been compared with any market evidence that may be available in relation to similar properties and the final valuation is in line with the valuation of other similar properties in Ontario.

 

## 3.0 The Valuation

### 3.1 Deriving the GIM

This method calculates an estimated stable gross income that can be generated by the motel by reference to market rates, then applies the GIM to arrive at a current value for the property.

GIMs and market rates are derived from information obtained from sales of motels and from annual operating statements and rent rolls reported by motel owners.

In simple terms, the formula for deriving the GIM is as follows:

GIM = Sale Price / Gross Annual Income

For example, if a motel that has revenues of $150,000 sold for $600,000, the GIM calculation would be as follows:

GIM = $600,000 / $150,000

In this example, GIM = 4.

This GIM could then be used in the valuation of other similar motels where the gross annual income has been calculated.

However, the actual gross income may require some adjustments before it can be used in a GIM calculation. The income needs to be stabilized, which requires that the revenues used in the valuation exclude any abnormal change in supply and demand, plus any temporary or infrequent conditions that may result in unusual levels of revenues or expenses to the property.

An example of this calculation is shown below:

| Derivation of Motel Gross Income Multiplier | | |
|---|---|---|
| **Item** | | **Amount** |
| Sale Price | | $3,500,000 |
| Motel Gross Income (Stabilized) | | $1,000,000 |
| Gross Income Multiplier | Sale Price/Gross Income | 3.50 |
| | | |

This GIM can then be used to value other motels using the same approach.

### 3.2 Data Qualification

The data collected must be qualified before it is used in the valuation process. Data qualification means that the data is verified by MPAC for:

 

- Accuracy – Is the information correct, or have any errors been made in reporting or recording it?
- Timeliness – Does it reflect the time period being analyzed?
- Appropriateness – Is the data representative of the type of motel being analyzed?

The data for an individual motel will be compared to the data obtained from similar motels to check that it properly reflects industry norms. This process is important to ensure that there is an equitable assessment base established for the valuation of all motels.

The income and other financial data will also be stabilized by MPAC, meaning that it should represent the typical performance that can be expected for any given year. Stabilizing the data also means that exceptional income or expenses in a particular year will be smoothed out to prevent distortion.

### 3.3 Data Classification

Motels range from small motels with few or no services to large, full-service luxury resort motels. The range of services and facilities provided in a motel, such as meeting rooms, swimming pools, exercise facilities, restaurants, convenience stores, etc., will affect the potential revenues and the costs of operating the property.

In addition to the costs of operation, the expertise demanded of management will also vary with the size and complexity of the property. The differences in revenues and expenses associated with the various types and sizes of motels, also produces a difference in the degree of risk associated with these properties.

For these reasons, it is important to ensure that only data appropriate to the particular type of motel concerned is used in the valuation process.

Because MPAC uses a GIM approach, the income used is not adjusted for vacancies or for operating expenses. Variations in these features are reflected in the use of a GIM, which reflects atypical situations in vacancy and expense levels.

### 3.4 Applying the GIM Approach

Having undertaken a detailed analysis of the financial performance of motels, and the available sales data, MPAC can proceed to value all motels using the GIM method.

MPAC's analysis of actual market sales, and the gross income of the motels that have sold, demonstrates the GIM for each transaction. For each sale, the gross income (and therefore the

 

GIM) will vary depending upon a number of factors, including the size, design, age, location and quality of the motel.

When valuing an actual motel, MPAC will use a GIM appropriate for the particular motel being valued. The GIM appropriate for the property will also depend upon a wide range of factors (i.e. size, design, age, location and quality). The GIM used will be considered in light of a comparison of the actual motel to the average or typical motel in the locality.

As already indicated, the value of a motel relates to its stabilized actual and potential performance.

While there are many motels of a similar nature, they will have different locations and often have different attributes, room mix, room finishes, restaurants, franchise affiliations, labour arrangements, market focus, etc. Therefore, in the valuation process, actual income forms the starting point in the process. This data will then be compared and tested to the performance of other motels and adjusted as appropriate in order to establish the assessment value.

These valuation parameters can then be compared to published industry data and fine-tuned to establish the industry norms or expected performance levels for a particular motel.

**Sources of Revenue**

Motels have a number of sources of revenue (for example, rooms, bars, restaurants, leisure facilities, etc.), which generate income and support the value of the entire motel enterprise. This income arises as a result of both tangible assets, such as land, buildings and personal property, and intangible assets, such as the brand and the quality of motel management.

The valuation of a motel for property tax purposes requires that the real estate portion be separated from the value of the other component parts, as only the real estate is subject to property tax.

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

Part of the revenue generated in a motel is attributable to FF&E. As FF&E are personal property and non-assessable, the value attributable to FF&E must be deducted from the final value generated by the gross income analysis. Section 45.3(2) of *Ontario Regulation 282/98*, states that unless the assessment corporation can demonstrate that the use of a different percentage is appropriate, the amount deductible in respect of personal property shall not exceed 15 per cent.

 

**Additions for Secondary Components Not Included in the GIM**

In most cases, motel properties tend to also contain residential living quarters for the owner/operator or there may be surplus land as part of the property, which, for a variety of reasons (e.g., market conditions) may be undeveloped. These secondary components must be valued separately and added to the current value of the property.

The determination of excess land involves a review of current zoning by-laws as well as the current density and configuration of the property. Excess land value is typically derived using market sales studies.

**Current Value**

Once the assessor has deducted the estimated value of the personal property from the adjusted gross income multiplied by the GIM, the remaining value is the current value of the motel.

Therefore:

(Adjusted Gross Income X GIM) – Personal Property= Value of the Motel

And:

Value of the Motel + Values of Any Additional Components to the Property =

Current Value for Property Tax Purposes

A sample valuation is provided in the next section.

## 3.5 Sample Valuation

| | |
|---|---:|
| Stabilized Adjusted Gross Income | $500,000 |
| Appropriate Gross Income Multiplier | 5.5 |
| Indicated Value | $2,750,000 |
| Personal Property | –$412,500 |
| **Motel Current Value** | **$2,337,500** |
| Value of additional property components | $200,000 |
| **Total Property Value** | **$2,537,500** |

### 3.6 Verifying the Results

Having completed the valuation using the GIM approach, MPAC's assessor will review the outcome to ensure that it is an accurate assessment of the current value of the property and is in line with the assessment of other similar motels.

### 3.7 Conclusion

This guide sets out how MPAC assessors approach the valuation of motels for property assessment purposes.

Although it outlines the general approach adopted, it does not replace the assessor's judgment and there may be some cases where the assessor adopts a different approach for justifiable reasons.

For further information about MPAC's role, please visit mpac.ca.