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D. GROOT LOGGING LTD.

v.

ASSESSOR OF AREA 25 - NORTHWEST

Supreme Court of British Columbia (A843319) Vancouver Registry

Before: MR. JUSTICE R.J. GIBBS (in Chambers)

Vancouver February 18, 1985

P.D. Feldberg for the Appellant
Robert Gill for the Respondent

Reasons for Judgment February 28, 1985

In *British Columbia Forest Products Limited* v. *Assessor of Area #03-Cowichan Valley; Prince George Pulp and Paper Limited* v. *Assessor of Area #26-Prince George*, (1984) unreported, Vancouver Registry Numbers A841788 and A841797, I held that the Assessment Appeal Board, acting under the provisions of the *Assessment Act*, R.S.B.C. 1979, Chap. 21, erred in law in disallowing a reduction, in determining the actual value of mill properties, in the face of uncontradicted evidence of the long term adverse impact of economic recession on the markets for the mill products.

In this case, decided on August 17, 1984, before my reasons issued in the BCFP and Prince George cases, the Board made the same error. At pages 6 and 7 of its decision the Board said:

> *External Obsolescence*
>
> It is further argued that unfavourable markets have diminished the value of the realty and the machinery, because a buyer would have had regard as at December 3 I, 1982, to the profitability of operating the plant.
>
> In this case the negative influences are the market conditions which, on the evidence, do not permit the subject to produce sufficient profit to service the long term debt required to construct it, nor to implement the Bison report findings at December 31, 1982.
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> The Board notes the decision of the Assessment Appeal Board in *Prince George Pulp* v. *Assessor of Area #26*, April 16, 1984. There the Board found that a cyclical downturn in the commodity market is not a permanent negative influence such as to constitute external obsolescence. The Board reasoned that a prudent purchaser would have regard to assumed market conditions over time and purchase on the substitution principle at an actual value that can be estimated by the cost approach. We are in respectful agreement with that reasoning, and have concluded that the additional 10% awarded by the Assessor is not justified nor does the Board accept the method of capitalizing the loss of business income from the sales of a commodity as advanced by the appellant.

In my opinion the Board here fell into the same error as did the Board in the *BCFP* and *Prince George* cases, in that they refused a reduction for external obsolescence due to unfavourable market conditions in the face of uncontradicted evidence of adverse market conditions. However, this case differs from the *BCFP and Prince George* cases in two major respects and cannot, therefore, be disposed of out of hand merely by applying the *BCFP and Prince George* cases.

The first major difference is in the treatment of an element of "functional" obsolescence. The Board clearly misunderstood the evidence on functional obsolescence. In order to appreciate the misunderstanding it is necessary briefly to trace the history of construction and production.

The plant, commonly referred to as the Northwest Panelboard Plant, is located at Smithers, B.C. It was constructed during 1980 and early 1981 at a cost of $12,840,932. It commenced operations in March, 1981. The plant is the only one of its kind in British Columbia. It utilizes waste wood residuals, shavings and sawdust, which would otherwise be disposed of by burning, to produce what is called "thin board" in panels under 1/4 inch in thickness. The competitive product is "lauan", an imported mahogany plywood.

The feasibility study, upon which construction of the plant was justified, projected a developing shortage in lauan supply, purchase of the entire thin board output by major panel manufacturers, a net return to the mill of $72 per thousand square feet of 1/8 inch thickness, and net annual sales of $8.7 million to $11.6 million. Reality fell far below expectations. Lauan supply increased; sales to major panel manufacturers could not be made in the face of lauan supply; the net returns to the mill were in the range of $40 per thousand square feet, less than 60% of the projections; and the financial statements show annual losses varying between $1 million and $3 million.

The plant also encountered technical problems. Design faults interfered with efficient production. Bison-North America Inc. were retained to devise corrective measures. They diagnosed the problems and recommended changes at a projected cost of $1,382,000 to increase efficiency. By the end of December, 1982 $125,000 had been spent but the owners concluded that because of the poor market for thin board further expenditures could not be justified.

The Board thought that implementation of the Bison-North America recommendations would eliminate the functional deficiency which prevented efficient production of "thick board" in the 1/4 inch to 3/4 inch thickness range. This is what the Board said at page 6 of its reasons:

> It is concluded that the improbable market conditions for the production of "thin board" constitutes a functional deficiency in the plant's design, layout and the type of machinery and equipment now in place. The expenditure of 1.25 million dollars, as recommended in the Bison report, is the cost to cure the functional deficiency which would allow the plant to produce the "thick board" in the most efficient manner. The value of the machinery and equipment is adjusted accordingly at the conclusion of this decision.

That quote discloses the misunderstanding. The Bison-North America recommended expenditure would merely have eliminated inefficiencies in thin board production. Had the expenditures been made the owners would have had an efficient thin board plant but an inefficient thick board plant because of functional deficiencies in connection with thick board production. The adjustment to value therefore does not reflect functional obsolescence for thick board production. But the highest and best use of the plant, according to the expert evidence, is the present mix of thin board and thick board production. The inefficiency in respect of thick board is twofold: problems in quality control; and the production line bottleneck created by a press used for thicknesses twice or more greater than the design thickness.

It was the Board's misunderstanding of the evidence that led it to the erroneous conclusion that implementation of the Bison-North America recommended expenditure would have led to the most efficient production of thick board. In my opinion, in order to reflect thick board inefficiencies a further reduction is required.

The second major difference is that in the *BCFP and Prince George* cases the owner and the assessor had agreed that the appropriate method of reflecting external obsolescence was reduction of actual value by a percentage factor. They had also agreed upon the percentage figure. In this case the assessor and the owner differ. The assessor would apply a 10% reduction; the owner contends for a reduction based upon capitalizing the loss of revenue attributable to reduced commodity sales. These submissions give rise to a fundamental question, namely; is the method of calculating a reduction in actual value to reflect external obsolescence a question of law for the court, or a matter within the jurisdiction of the Board?

The answer to the question requires reconciliation of apparently conflicting decisions. The starting point, is the basic principle found in the judgment of the Chief Justice in *Dreifus* v. *Royds* (1922) 64 SCR 346 at pages 348 and 349:

> I am of the opinion that in a question of this kind as to the "actual value" of lands for purposes of assessment this court would not and should not interfere with the finding of fact as to such "actual value" if there was any evidence to sustain that finding. The Board is constituted of men of experience on questions of this character. They have the great advantage of visiting and viewing the lands in question, and of seeing and hearing the witnesses who may be called to speak of its value. Unless, therefore, the Board misdirected themselves on the proper principles which should govern them in determining this "actual value", or obviously reached their conclusions as to such value by adopting and following some wrong or improper principle, this court would not and should not interfere with their findings.

Proceeding from that basic principle, the conflict, if indeed there is one, appears from a judgment of the Court of Appeal in 1963 when placed alongside a judgment of my brother Meredith in 1979, followed by Chief Justice McEachern in 1981.

In 1963, in *Provincial Assessors of Comox, Cowichan and Nanaimo* v. *Crown Zellerbach et al.* (1963) 42 WWR (NS) 449 (BCCA), at pages 455 and 456, Davey, J.A. held that:

> The statutory duty of the assessor is to find the "actual value" of the taxable property, but sec. 37 permits him to use several different methods and to consider many different elements in finding actual value. I do not think that the use of any specifically mentioned method of finding actual value, or the inclusion or exclusion of any enumerated element, provided there is evidence to support the reasoning, can be said to raise a question of law appealable to the courts on a stated case, for those matters lie in the judgment of the assessor and the assessment equalization board: *Reg.* v. *Penticton Sawmills Ltd.* (1954) 11 WWR (NS) 351, at 353, 356.
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> (The emphasis is mine).

On the other hand, in an unreported portion of his reasons in *Swan Valley Foods Ltd.* v. *Assessment Appeal Board* (1979) 13 BCLR 304, Meredith, J held that:

> The question of whether the selection of any given method of assessment is wrong in principle is a matter of law, not fact.

In *Western Indoor Tennis* v. *Assessor of Area 11, Richmond-Delta* (1981) 29 BCLR 265 McEachern, C.J applied the *Swan Valley Foods* statement of the law.

In my opinion, the reconciliation of the cases is to be found in the words "provided there is evidence to support the reasoning" in the above quote from Davey, J.A. in *Crown Zellerbach*. In the *Swan Valley Foods* case there was no evidence to support the method selected and so the Board was wrong in principle. That is also the foundation for the decision in *Western Indoor Tennis*.

I conclude, on the basis of the above, that the answer to the question is that providing the Board selects a method from section 26 (3) and (3.1) of the Act, and providing there is evidence upon which to base the method arid the reasoning followed in applying it, the Board will have acted in accordance with its statutory powers and duties, and the court will not intervene. Because the appellant's plant is unique and encounters marketing problems attributable to other factors in addition to those that other industries in the area have encountered due to the general economic recession, it seems to me that this is a case where a generally employed percentage reduction for the geographic area would not be an appropriate method for calculating economic obsolescence.

Returning now to the stated case, the questions for the opinion of the court and the disposition thereof is as follows:

> 1. Was the Board's conclusion that "the expenditure of 1.25 million, as recommended in the Bison Report, is the cost to cure the functional deficiency which would allow the plant to produce the 'thick board' in the most efficient manner" contrary to all the evidence and therefore an error in law?
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> Answer: Yes.
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> 2. Was the Board's decision that no external or economic obsolescence exists in the plant contrary to all the evidence and therefore in law?
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> Answer: Yes.
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> 3. Was the Board's decision not to accept the appellant's method of capitalizing the loss of business income to estimate external or economic obsolescence an error in principle and therefore in law?
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> Answer: No, providing there is evidence to support it, the Board may select any of the section 26 (3) and (3.1) methods that is appropriate.
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> 4. Was the Board's conclusion that the negative factors affecting the plant were due to a cyclical downturn in a commodity market contrary to all the evidence and therefore an error in law?
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> Answer: Yes.
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> 5. Was the Board's decision that the actual value of the plant was unaffected by the negative economic factors facing the plant an error in principle and therefore an error in law?
>
> Answer: Yes.

In accordance with section 74 (6) of the Act, these reasons will be remitted to the Board as the opinion of the Court.