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B.C. TIMBER LTD.(WESTAR TIMBER LTD.)

v.

ASSESSOR OF AREA 25 - NORTHWEST

Supreme Court of British Columbia (A843321) Vancouver Registry

Before: MR. JUSTICE B.D. MACDONALD (in chambers)

Vancouver April 1, 1985

B.J. Wallace and Peter Feldberg for the Appellant
Robert S. Gill for the Respondent

Reasons for Judgment April 9, 1985

At the request of the parties, the Assessment Appeal Board of British Columbia (the "Board") has submitted a Stated Case seeking the opinion of this court under s. 74 of the *Assessment Act*, R.S.B.C. 1979, c. 21 (the "Act") on certain questions arising out of two decisions of the Board. Both decisions are dated November 1, 1984. One relates to a sawmill in Terrace and the other to a pulpmill at Prince Rupert, both of which are owned by the appellant.

While the Stated Case sets out a total of thirteen questions, including two stated at the request of the respondent, counsel agree that there is considerable overlap and that all can be answered by the resolution of five issues. They are:

1. Did the Board err in refusing to deduct from the estimated cost of construction an amount for excess operating costs in determining the actual value of both the sawmill and the pulpmill?

2. Did the Board err in failing to deduct an allowance for external obsolescence in both cases?

3. Did the Board err in refusing to include interest during construction in the estimated costs of construction in the process of valuing both mills by the cost approach?

4. Did the Board err in refusing to admit certain rebuttal evidence tendered by the appellant in the sawmill case?

5. Did the Board err in taking judicial notice of the facts found and its own conclusions thereon in its prior decision between other parties in *Crown Forest Industries Limited* v. *Assessor of Area #06 – Courtenay,* dated September 14, 1984?

The relevant portions of the governing sections in the Act are:

"26. (1) The assessor shall determine the actual value of land and improvements.

(2) In determining the actual value. . . the assessor may give consideration to the present use, . . . cost of replacement. . . and any other circumstances affecting the value, . . .

(3) . . . where an industry. . . is carried on, the land and improvements so used shall be valued as the property of a going concern.

74. (2) A person affected by a decision of the board on appeal. . . . may require the board to submit a case for the opinion of the Supreme Court on a question of law only. . ."

"Actual value" in s. 26 means market value, but because comparable sales of sawmills and pulpmills are almost non-existent, the alternative most often used by appraisers is the "cost approach". The Board employed that method in the two decisions in question here. The cost approach seeks to determine what a prudent purchaser would pay to replace the property in its present condition. The cost to reproduce the mill is estimated and then allowances are made for such items as obsolescence, physical deterioration and external factors.

EXCESS OPERATING COSTS AND EXTERNAL OBSOLESCENCE

Issues 1 and 2 stated above are easily resolved. The Board did not have the benefit on November 1, 1984 of the following decisions of this court on three appeals involving these issues:

(a) *B.C. Forest Products* v. *Assessor of Area #3 - Cowichan Valley*, and *Prince George Pulp and Paper* v. *Assessor of Area #26 - Prince George* (unreported; Vancouver Registry Nos: A841788 and A841797; November 2, 1984).

(b) *B.C. Timber Ltd.* v. *Assessor of Area #18 - Trail-Grand Forks* (unreported; Vancouver Registry No. A841323; February 8, 1985).

(c) *D. Groot Logging Ltd.* v. *Assessor of Area #25 - Northwest-Prince Rupert* (unreported; Vancouver Registry No. A843319; February 28, 1985).

On the basis of those decisions, by which I am bound and with which I agree, the Board erred in both its decisions in question here in failing to deduct from the estimated replacement costs amounts for excess operating costs and external obsolescence. It is clear on the authorities that both those errors (in the application of "appraisal principles") are errors in law and thus within the jurisdiction of this court under s. 74 of the Act.

The Board purported to rely on facts which it had earlier found in another of its decisions (*Crown Forest Industries* v. *Assessor of Area #06 - Courtenay* - September 14, 1984) to support its conclusions in the two decisions now before the court on both issues (excess operating costs and interest during construction). For the reasons expressed below in discussing issue 5, the Board was not entitled to do so. The respondent concedes that the Board cannot apply facts found in another case and peculiar to it, to the decisions in question here.

The respondent does not contend, in the face of the three decisions of this court listed above, for any different result on issues 1 and 2 than that the Board erred in law. Quite properly, the respondent points out that it will be up to the Board to fix the quantum of the deductions to be made from replacement costs for both those factors in connection with both mills, based on the evidence before it in each case. Those are questions of fact for the Board to decide.

INTEREST DURING CONSTRUCTION

Issue 3 (interest during construction) is one raised by the respondent. The Assessor sought to add interest on 50% of the estimated replacement cost of both mills over the estimated time which would be involved in their reconstruction (to reflect the cost of progressive advances of construction expenditures over that period). The Board rejected that approach, relying on the facts found in its earlier decision in *Crown Forest Industries* to do so. While the appellant agrees that such reliance was an error in principle on the part of the Board, it supports the Board's conclusion on other grounds. The stated case, on this issue, could be answered on the basis that

the Board erred in taking judicial notice of its own decision in Crown Forest Industries, but that would not provide the Board with this court's opinion on the issue of whether interest during construction should be added to construction costs. That in turn will invite another stated case in due course. I have decided to answer the question fully.

Both parties presented evidence to the Board of the percentage which should be added to the estimated construction costs to represent interest during construction. The respondent suggested 15%; the appellant 6%. In argument before the Board however, the appellant took for the first time the position which it advances here. The appellant submits that nothing should be added for interest during construction, despite the evidence of its own appraiser, because such an addition is designed to offset the advantage of the immediate revenue which is available on the purchase of an existing mill. The relative benefits and burdens of having a mill on stream on day one, the appellant argues, cannot be weighed without a sophisticated present value analysis, which appraisers (and the Assessor here) did not do. Thus the appellant submits that because appraisers do not concern themselves with "incidental losses" generally, they should not deal with this particular issue in isolation; interest during construction should be regarded as a set-off against incidental losses.

That approach is suggested in *Bonbright on The Valuation of Property,* a treatise on the appraisal of property for different legal purposes (at pages 161 and 162):

> "If appraisal were as scientific a procedure as it can be made to appear on paper, these time-discount factors would require specific allowance. . .
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> At best, however, appraisal is subject to extremely wide margins of error. . . Indeed. when substitute property can be bought on the open market or quickly manufactured to order, no allowance whatever is usually made for time discount.
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> . . .
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> What is especially striking, however, is the fact that in large appraisals based on the estimated reproduction costs of plants that require a year or more for completion, most appraisers allow for the interest factor in a way that would seem directly opposed to the one just suggested. Instead of discounting the prospective construction outlays, they add an allowance for interest during construction. sufficient to compensate the owner for funds advanced prior to the date as of which he may enter and operate the plant."

I pause to comment that this is exactly what both the Assessor and the appellant's appraiser did (to different degrees) in their evidence before the Board. Mr. Bonbright continues:

> "The subject deserves far more discussion than it has yet received from the appraisal engineers. But the author surmises that the reversal of the interest factor in favor of a higher valuation is taken as a partial offset to the omission of the incidental-loss factor. Appraisers, one must remember, seldom deem themselves qualified to estimate incidental losses. They may therefore rest content to treat these losses as if they were equal to interest during construction."

That passage, and in particular the last sentence thereof, is the basis on which the appellant argues that nothing should be added to the estimated costs of construction for interest during construction. I have some reservations as to whether the passage quoted supports that argument.

The respondent meets the appellant's argument with two submissions. First, the Assessor here (and for that matter the appellant's appraiser as well) simply followed the course which "most appraisers" adopt. That approach, Mr. Bonbright's apparent view to the contrary notwithstanding, is common both here and in the United States. In *Commissioner of Transportation* v. *Willett*

Holding Company (1972) 298 Atlantic Reporter (2d) 69 (S.C. of New Jersey), the following appears:

> "[3] It seems well settled that in addition to direct outlay for labor and materials, replacement or reproduction cost will normally include financing charges. These may take the form of interest payments actually made as well as interest calculated on equity investment during the construction period.
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> . . .
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> There is, . . . , a logical inconsistency in not employing the reproduction cost method throughout. As to items of expense other than the financing charges, consistent use was made of actual costs. . . . The same should have been done with the financing charges. . . ."

The point is made even more forcefully in *City of New York* v. *Salvation Army* (1978) 373 N.E. Reporter (2d) 984 (C. of A., N.Y.) at p. 985:

> "Implementation of the summation method requires the inclusion not only of payments for material, equipment, labor and other obvious physical ingredients which go directly into construction, but also of those charges which may be termed indirect or less direct, such as architects' fees, contractors' profits, interest and taxes on land value during the period of construction, cost of procuring necessary licenses and the miscellany of other essential overhead or incidental expenses. For a fair and realistic appraisal of reproduction costs must embrace in its reckoning all expenditures that reasonably and necessarily are to be expected in the re-creation of a structure so idiosyncratic as to leave no alternative method by which to measure fair compensation.
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> . . .
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> Financing costs are such an expenditure. . . Commonly, an owner will make payments to a contractor from the proceeds of a loan it will have secured for financing the work: clearly the lender's charges will he just as real an expense to the borrower as the dollars it pays to its contractor. Such costs will be no less real when an owner employs its own capital: it thereby foregoes its earning power by turning it into an equity investment which rarely will produce income during construction. . . Thus, whether an owner uses its own or borrowed funds, the calculation of true cost would, either way, require inclusion of the costs of financing."

The second submission of the respondent on this issue arises out of the following passage on p. 8 of the decision of my brother Gibbs in the *D. Groot Logging Ltd.* case referred to above:

> ". . . the answer to the question (whether a reduction for external obsolescence is a question of law or a matter within the jurisdiction of the Board) 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 and 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."

In applying that passage to these cases, the respondent submits that the appellant is asking this Court to weigh the evidence; to resolve a question of fact. Whether the "cost approach" is an appropriate method of determining actual value is a question of law the respondent says, but what factors are to be considered in applying that approach are for the Board, provided there is evidence to support its reasoning.

I reject in part that second submission of the respondent. Provided there is evidence before it on the question of interest during construction, the Board is bound to decide what amount should be added to the estimated cost of construction to reflect that factor. I find myself unable to distinguish between the "appraisal principles" of excess operating costs or external obsolescence on the one hand and the "theory" of interest during construction on the other. The rejection by the Board of any of those three "principles" is an error in law.

I have concluded that the Board was wrong in rejecting the inclusion of interest during construction on the basis which it did (judicial notice of its facts and conclusions in Crown Forest Industries). In principle, the Board is obliged to include in its calculations an allowance for that expense. Whether or not the Board does so in a given case must depend upon the evidence before it. I have not analysed the evidence in these cases, but from what the parties said on this hearing, it would appear that the issue before the Board in this case is "how much?" rather than "whether or not?".

REBUTTAL EVIDENCE

The respondent concedes that the rebuttal evidence in question was not available to the appellant until after the hearing and that such evidence was contradictory of evidence on which the Board apparently relied in reaching its decision in the sawmill case. However, the respondent submits that the admission of such evidence, where it would make no difference in the outcome, is entirely discretionary (see: *Mersey Paper Co. Ltd.* v. *County of Queens* (1959) 18 D.L.R. (2d) 19 (N.S.S.C.-C.A) at p. 36).

The Board's reasons for rejecting the rebuttal evidence ("new evidence is not acceptable in final argument when the respondent has met the case") are completely unsatisfactory. However, a consideration of the rebuttal evidence which was tendered and a perusal of the Board's reasons in the sawmill case, together with the respondent's argument that the rebuttal evidence goes to an event which occurred eighteen months after the December 31, 1982 date as of which the actual value of the sawmill was to be determined under the Act, all lead me to conclude that the respondent's submission on this issue must be accepted.

I find in the circumstances here that the Board had a discretion whether or not to accept this particular evidence. The Board thus cannot be criticized for rejecting it.

JUDICIAL NOTICE

On the questions of excess operating costs and interest during construction, the Board in both these cases took judicial notice of the facts and conclusions in its earlier decision in *Crown Forest Industries*. Both parties argue that it was improper for the Board to do so. I agree.

When the Board proceeds in such a fashion the parties have no means of testing the alleged evidence in those other proceedings. While ultimately a board may apply to its final administrative decisions certain policy considerations, this portion of the Board's decisions was part of its quasijudicial function. Where the Board seeks to rely on information gathered by it outside the hearing, it ought to allow that information to be tested in the hearing before relying on it. (see *Township of Innisfil* v. *City of Barrie* (1978) 7 O.M.B.R. 233 (Ont. H.C. Div. Ct.), aff'd 95 D.L.R. 298 (Ont. C.A.).

I accept the appellant's argument that the Board's power to take judicial notice of facts is limited to matters so generally known and accepted that they can be readily verified and cannot reasonably be questioned. All the evidence before it on the two questions which the Board decided in these cases by taking judicial notice of its own former decision in *Crown Forest Industries* was contrary to the Board's conclusions in that case. The Board should not have done so without at least having first ensured that the parties were given a full opportunity to meet and deal with such evidence.

I express no opinion, in light of my limited understanding of the evidence which was before the Board in *Crown Forest Industries*, as to whether even adequate prior notice would enable the Board to proceed in the manner which it did.

ANSWERS TO QUESTIONS STATED

The answers to the questions stated for the opinion of the court are:

Questions on the Sawmill Appeal:

1. Did the Board err in principle and therefore in law in refusing to deduct an amount for excess operating costs related to the Sawmill in determining its actual value pursuant to section 26 of the *Assessment Act*?

ANSWER: YES

2. Did the Board err in principle and therefore in law in refusing to deduct an amount as an economic allowance in determining the actual value of the sawmill pursuant to section 26 of the *Assessment Act*?

ANSWER: YES

3. Did the Board err in law in refusing to accept the deduction for an economic allowance as proposed by the appellant and the respondent when the only evidence before it was the appellant's and respondent's evidence that such a deduction was appropriate in the circumstances?

ANSWER: YES

4. Did the Board err in law in taking "judicial notice" of the facts and conclusions in the appeal of *Crown Forest Industries Limited* v. *Assessor of Area #06-Courtenay* to reach its conclusion that excess operating costs are not a factor to be considered in the determination of actual value by the cost approach?

ANSWER: YES

5. Did the Board err in law in concluding that a penalty for excess operating costs was not to be deducted from the value of the Sawmill otherwise determined by the cost approach when the only evidence before the Board was that a penalty for excess operating costs was appropriate?

ANSWER: YES

6. Did the Board err in law in refusing to admit the evidence of the appellant tendered by way of affidavit to rebut the evidence that dry kilns were used in the West Fraser/Skeena sawmill to process lumber on a dimension cut basis?

ANSWER: NO

Questions on the Pulpmill Appeal:

1. Did the Board err in principle and therefore in law in refusing to deduct an amount for excess operating costs relating to the Pulpmill in determining its actual value pursuant to section 26 of the *Assessment Act*?

ANSWER: YES

2. Did the Board err in principle and therefore in law in refusing to deduct an amount as an economic allowance in determining the actual value of the Pulpmill pursuant to section 26 of the *Assessment Act*?

ANSWER: YES

3. Did the Board err in law in refusing to accept the deduction for an economic allowance as proposed by the appellant and the respondent when the only evidence before it was the appellant's and respondent's evidence that such a deduction was appropriate in the circumstances?

ANSWER: YES

4. Did the Board err in law in taking "judicial notice" of the facts and conclusions in the appeal of *Crown Forest Industries Limited* v. *Assessor of Area #06-Courtenay* to reach its conclusion that excess operating costs are not a factor to be considered in the determination of actual value by the cost approach?

ANSWER: YES

5. Did the Board err in law in refusing to make any deduction for excess operating costs and an economic allowance when the only evidence before it was the evidence that such deductions were appropriate in the circumstances?

ANSWER: YES

Questions stated at the request of the respondent:

1. Did the Assessment Appeal Board err in law in failing to allow external obsolescence as agreed by the assessor (respondent) and the appellant?

ANSWER: YES

2. Did the Assessment Appeal Board err in law in taking judicial notice of the facts and conclusions in the decision of *Crown Forest Industries Limited* v. *Assessor of Area #06-Courtenay* in failing to allow excess operating costs and interest during construction?

ANSWER: YES

In accordance with s. 74 (6) of the Act, these reasons will be forwarded to the Board as the opinion of the court.