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**CROWN FOREST INDUSTRIES LIMITED**
**(formerly Crown Zellerbach Canada Limited)**

**v.**

**ASSESSOR OF AREA 6 - COURTENAY**

Supreme Court of British Columbia (A843031) Vancouver Registry

Before MADAM JUSTICE M.F. SOUTHIN

May 6,7,8,9 and 10, 1985

Written Argument Submitted by the
Appellant dated 5th June, 1985
Written Argument Submitted by the
Respondent dated 8th June, 1985

Brian J. Wallace and Peter Feldberg for the Appellant
John E.D. Savage for the Respondent

**Reasons for Judgment** August 8, 1985

In this appeal by way of stated case from the determination of the Assessment Appeal Board that certain property, real and personal, owned by the appellant at Elk Falls, which I shall call "the lands" had an "actual value" of $429,537,000.00 in 1982 for purposes of taxation in 1983 and not $264,250,000.00 as the appellant asserts, the appellant must persuade me that the Board erred in law. The respondent assessor also seeks to persuade me that the Board erred in law but the questions posed by the assessor are a minor part of this, to me, intellectually elusive case.

PART 8
STATED CASES AND APPEALS ON MATTERS OF LAW

Procedure on appeal on law to Supreme Court

> 74. (1) At any stage of the proceedings before it, the board, on its own initiative or at the request of one or more of the persons affected by the appeal, may submit, in the form of a stated case for the opinion of the Supreme Court, a question of law arising in the appeal, and shall suspend the proceedings and reserve its decision until the opinion of the final court of appeal has been given and then the board shall decide the appeal in accordance with the opinion. (underlining mine)

I accept that part of my difficulty comes from my lack of experience in this esoteric branch of the law. Although determining "actual value" for assessment bears some resemblance to determining value in expropriation proceedings or damages in actions concerning breaches of contract on the sale of lands, counsel and the judge in such cases do not have to worry about the lines between questions of law, questions of fact and questions of mixed law and fact.

While part of my difficulty is my own lack of experience, much of that difficulty comes from the applicable statute-the *Assessment Act* R.S.B.C. 1979 c. 21 which, while suitable enough for valuing the house on the corner or the dairy farm in the Fraser Valley or even the Pacific Centre,

is woefully lacking in standards for valuing the lands of a large integrated forest concern which is spread over many assessment districts.

The statute says only this:

PART 3

VALUATION

Valuation for purposes of assessment

> 26. (1) In this section "actual value" means the actual value that land and improvements would have had on July 1 had they and all other land and improvements been on July 1 in the state and condition that they are in on September 30 and had their use and permitted use been on July 1 the same as they are on September 30;
> "September 30" and "July 1" mean
>
> (a) in relation to an assessment roll completed as required by section 2 (1), September 30 and July 1 of the year during which the assessment roll is completed, and
>
> (b) in relation to a revised assessment roll completed as required by section 2 (1.1), September 30 of the year during which the revised assessment roll is completed, and July 1 of the year immediately before that.
>
> (2) The assessor shall determine the actual value of land and improvements and shall enter the actual value of the land and improvements in the assessment roll.
>
> (3) In determining actual value, the assessor may give consideration to present use, location, original cost, replacement cost, revenue or rental value, market value of the land and improvements and comparable land and improvements, economic and functional obsolescence and any other circumstances affecting the value of the land and improvements.
>
> (3.1) Without limiting the application of subsections (1) to (3), where an industrial or commercial undertaking, a business or a public utility enterprise is carried on, the land and improvements used by it shall be valued as the property of a going concern.

As will become apparent, this fleshless skeleton of a statute has driven the parties in this case and has driven them in others concerning pulp mills to use theories of valuation which are nothing more than unproven hypotheses of the behaviour of economic man. As a lawyer accustomed to dealing in the legal consequences of fact substantiated in evidence or facts of which judicial notice can be taken, I find it astonishing to be told that various hypotheses (called appraisal theory) are principles of law.

To say that an unproven hypothesis of behaviour is factually true is, in itself, difficult to swallow but I find it next to impossible to swallow that such an hypothesis can be elevated to a proposition of law.

The proposition, however, was recently enunciated by Macdonald, J. of this Court in these words:

> 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 <u>that both those errors (in the application of "appraisal principles")</u> are errors in law and thus within the jurisdiction of this court under s. 74 of the Act.
> (underlining mine)

*B.C. Timber Ltd.* v. *Assessor of Area 25-Northwest* Vancouver Registry No. A843321 9th April, 1985 unreported and referred to and followed by McKay, J. in *MacMillan Bloedel Limited* v. *Assessor of Area 07-Sunshine Coast* Vancouver Registry No. A843323 15th July, 1985 at p. 19.

As the case before me also raises issues of external obsolescence and excess operating costs, both counsel urged the judgment of Macdonald, J. upon me. However, the passage quoted makes no sense to me and I cannot write reasons for judgment founded upon something which makes no sense. It may well make sense to the Court of Appeal. With that cri de coeur, I turn to the matters in issue.

A. THE LANDS BEING ASSESSED AND THE MARKET EVIDENCE OF VALUE

The appellant is a large integrated forest company which, in addition to the complex of a pulp and paper mill and sawmill at issue owns mills on the Mainland of British Columbia, extensive timber lands with their logging roads and so forth and other assets throughout British Columbia. At Elk Falls, which is near Campbell River, British Columbia, it produces newsprint, pulp, kraft paper and lumber.

I infer from the evidence that at all material times the pulp mill was in operation. These mills do not run themselves; they are run by a labour force with a general manager at the top, clerical and technical staff, operating crews, tradesmen and so forth. The pulp and paper mill is described as producing newsprint from processes known as thermal mechanical pulping for 85% of rated capacity and chemical thermal mechanical pulping for 15% of rated capacity. The sawmill is a state of the art dimension lumber sawmill and planer mill facility. (The Board's judgment, page 3.)

Unlike the other appeals of assessments relating to pulp mills which have recently been heard in this Court, in this appeal there was a market sale to assist the Board in its deliberations, not to be sure a sale of the lands being assessed but a sale of 96% of the shares in the owner of the lands and other assets, Crown Zellerbach Canada Ltd. by its parent, Crown Zellerbach International Inc., to Fletcher Challenge Holdings (Canada) Ltd., a subsidiary of Fletcher Challenge Ltd., a rising multinational born in New Zealand.

Those shares were purchased in late 1982 for approximately $533 million.

The first issue before the Board and its determination of which is not the subject of appeal by either party, was whether the share transaction was something which could be looked at in determining the actual value of the lands.

The Board approached this by asking itself whether the sale was a "market sale" and, on the evidence, answered, "yes".

B. A GLOSSARY OF TERMS USED IN THE PROCEEDINGS

*Reproduction Cost:* The cost of construction at current prices of an exact duplicate or replica using the same materials, construction standards, design, layout, and quality of workmanship, embodying all the deficiencies, superadequacies and obsolescence of the the subject building. (Board's judgment: Page 10)

*Replacement Cost:* The cost of construction at current prices of a building having utility equivalent to the building being appraised but built with modern materials and according to current standards, design and layout. The use of the replacement cost concept presumably eliminates all functional obsolescence, and the only depreciation to be measured is physical deterioration and (economic) external obsolescence.
(Board's judgment: Page 10)

*Cost Approach:* A method of appraisal founded on the "principle of substitution:" The principle of substitution is basic to the cost approach. The principle affirms that no prudent investor would pay more for a property than the amount for which the site can be acquired and for which improvements that have equal desirability and utility can be constructed without undue delay. Older properties can also be substituted for properties being appraised and their value is relative to the value of new optimal property.
(Evidence of Thomas Johnstone: Volume VII page 761)

*Allocation of Share Purchase Price by Earnings:* This is a method of appraisal by which the appraiser determines what income comes from what asset and then allocates the purchase price in the same proportion as the income from an asset bears to the total income.

*Income Approach:* All methods of valuation dependent upon the analysis of an income stream.

*Discounted Cash Flow Analysis:* In this method future cash flows derived from the sale of the products of the lands being assessed and the costs of their production are estimated to determine whether or not the net income projected can sustain the capital investment required to produce the cash flows at an appropriate rate of return.

*Incurable Functional Obsolescence (another term for it is "Excess Operating Costs"):* In cost approach theory, the difference in operating costs between a modern state of the art mill and an older mill with the same capacity. The argument goes that the older mill is less efficient and requires more persons to operate it.

*External Obsolescence:* In cost approach theory, the diminished utility of the subject of assessment due to negative influences from outside the site.
(Board's judgment: Page 16)

*Interest During Construction:* In cost approach theory, this is the assumed interest which the investor would have to pay on the money he was putting into the project before it came into production.
(Evidence of Thomas Johnstone: Volume VII page 763)

C. THE PROCEEDINGS BEFORE THE ASSESSMENT APPEAL BOARD

The appeal from the decision of the Court of Revision came on before the Assessment Appeal Board on the 28th May, 1985, and occupied in total seventeen days, including a day in San Francisco taking the evidence of an officer of Crown Zellerbach as to its reasons for selling. The exhibits number 34, one of which, exhibit 1, is several hundred pages long.

In the course of the hearing the chairman said:

> The Chairman: Because what this Board is going to do is settle a whole bunch of questions once and for all. The Board's going to use all 3 approaches to value and - going to tell you whether any of this stuff, this theory all applies or it doesn't apply and we're going to settle it once and for all in one appeal.
>
> Mr. Wallace: Why me?
>
> The Chairman: It's not only you. It's the whole industry and the whole Assessment Authority and it's been going on for 2 years and this is a chance to get it and that's why we're pushing to get this appeal to an end. And you can all go to court and settle the whole thing!

The chairman, I fear, may be overly optimistic.

Because the questions posed raise issues of evidence or no evidence and of the reasonableness of the Board's conclusions, I consider it unfortunately necessary to give a summary of the proceedings.

The appellant began the appeal by submitting a volume, exhibit 1, which contains, among other things, annual reports of Crown Zellerbach (Canada) Ltd., annual reports of Fletcher Challenge Ltd., various documents prepared in accordance with the search by Crown Zellerbach for a purchaser and contract documents for the sale.

*The Case for the Appellant*

a) James Christensen, the former manager of the Elk Falls complex and now vice-president of the pulp and paper group: A study in 1979 showed a shortage of newsprint and, therefore, Crown Zellerbach and other forest companies installed more paper making capacity. Crown Zellerbach installed its No. 5 paper machine. The recession began in the spring of 1982 and the price fell $80.00 per ton. The cost of building a pulp mill is such that nobody would build one now. Forecasts are suggesting that lumber may never come back. In 1977-82, the company spent some $50 million at Fraser Mills (on the Mainland). A "green field" mill, Le., a new mill on an empty site of the same capacity as Elk Falls could cost between $500 million and $600 million and could go to $800 million.

(b) Lawrence Carl Ryan, President and Chief Executive Officer of Crown Forest Industries Ltd. who is a New Zealander and a Director of Fletcher Challenge: The dominating factor in the purchase of the shares was the earning capacity - earnings records and earnings prospects. Fletcher Challenge wanted a real after tax rate of return (i.e., after inflation) of 6 per cent. The parties made no allocation of the purchase price of the shares for the various assets. The depreciated replacement cost of the mill is $585 million. D.R.I. (a forecasting service) is a standard source in the industry for making investment analyses and so forth but it is overly optimistic.

(c) Dr. Garrick Ewart Styan (Volume II - 30th May, 1985). Pulp and paper is an international commodity. Canada is a major supplier in the world of newsprint. There were good conditions in the industry in the 70's and into 1980. In the early 80's there was a down turn. Canada was also affected by currency devaluations by her competitors, particularly Sweden. In 1981 and 1982 there was a 35 per cent increase in newsprint capacity in British Columbia. Long term prospects are poor unless there is a "change in product profile". He prepares market analyses for the forest industry on a discounted cash flow basis using D.R.I. data as a base but adapted to real dollars.

(d) Affidavit of Ian Hudson. The reproduction cost in 1982 of things installed at the site over the years is some $911 million. It must be noted, however, that it is not clear whether everything on his list still existed in 1982 or whether there are items comprised in it of no present utility.

(e) Paul Raymond Williams: Assistant Corporate Controller of the appellant who gave evidence as to the plaintiffs two theories - the one being an allocation of the share purchase price by book value and the other, a discounted cash flow analysis.

(i) *Allocation Method*

The allocation of a share purchase price is on the basis of one hundred per cent of the shares at $33.00 per share, although Fletcher Challenge only obtained 96 per cent of the shares. After calculation of the value of the tax shields the true purchase price for all the assets of the company was $592 million and for all properties, i.e., buildings, machinery, equipment, timber lands and other lands

was $512 million. The total book value of the same properties was $527 million and thus, the purchase price was 97 per cent of the book value of those assets. As the book value of the lands under assessment is $321 million the amount properly ascribable to Elk Falls is 97 per cent of that amount or, $312 million (page 249 - Volume Ill).

*(ii) Discounted Cash Flow* Analysis

The purpose is to establish a net present value from future cash flows for the facilities that existed at 31st December, 1982. Exhibit 1 - C-l contains the calculations. The top sheet of the exhibit is a summary page which gives the incremental cash flows that are projected to be derived from that mill. There are a series of numbers which are used from which to develop volumes and realisations and costs that are estimated to be incurred in the future. The eventual development of cash flow information has to be driven by a number of things and certain assumptions about prices and costs and volumes. Much of the data for price and cost forecasting comes from Data Resources Incorporated. A forecast tax rate is used, in this case, 45 per cent. Inherent in the forecast is an assumption that there will be no change in tax legislation or rates. Having finally arrived at net cash flow a discount factor must be applied and the one chosen was 15 per cent because it is in use for investments within the forest industry. On that basis the net present value is $341 million.

Other evidence indicated that if a discount rate were 17 per cent the indicated value was $295 million (see page 969 in the Volume of 30th July, 1984).

(f) William Douglas Grant who gave evidence on the 4th June, 1984, is the assistant resident manager of the Elk Falls mill; from 1973 until he became assistant resident mill manager he was the plant engineer. He gave evidence of the state of the mill and various work that has been done on it and is thought to be necessary, i.e., curable physical depreciation and then turned to incurable functional obsolescence in the form of ongoing excess operating costs. As to that, Mr. Wallace said to the Board, "The assessor and the appellant have come to basically the same conclusion with respect to those excess operating costs with one significant exception. . .; that question being whether or not the calculation should take place before or after tax" (page 291). At page 312 the chairman said, "OK the parties agree, $120 million excess operating costs before tax. "It then became apparent that if the deduction is an after tax figure the amount of excess operating costs would be $64.8 million.

At p. 315, Mr. Wallace for the appellant said:

. . . as I indicated in my opening, we do not rely on the cost approach. . . however, that is not to say that there won't be some evidence on - there is going to be evidence on the cost approach from the assessor; I intend to cross examine on that evidence and I may wish to call evidence to rebut some of that evidence.

(g) David Lane gave evidence on the 5th June, 1984, (page 322, Volume IV). He is an expert appraiser and real estate valuer whose appraisal is exhibit 15. At page 324,

In addressing a problem, we've reviewed appraisal <u>theory</u> and valuation and the valuation process at the outset and included some text authorities with our report which outline contemporary valuation <u>theory</u>. (underlining mine)

The appraiser should put himself in the shoes of the probable purchaser in the specific sub market (i.e., in this case the potential purchasers of pulp mills) and do the appraisal using the type of criteria and value rationale which vendors and purchasers use in that specific market. The

cost approach is "non-market related" (page 335). The development of a detailed value by way of the cost approach tends to become a non-market oriented, academic exercise. "In the market place the cost approach is not given a great degree of consideration by the purchaser. He is looking to acquire cash flows. "On the basis of discounted cash flow the value is $341 million and by analysis of the sale $285 million. At page 4 of his report:

> In estimating the property's actual value by way of the income approach historic and projected operating results have been reviewed. These operating results and projections have been based on information compiled by Data Resources Incorporated (D.R.I.) D.R.I. information is utilized by the majority of British Columbia producers and is further utilized by industry on a worldwide basis. The D.R.I. information represents base data which the most probable purchaser(s) would consider in rationalizing an acquisition or disposal decision. During the past six months working closely with Mr. P. Williams, numerous D.C.F. calculations have been completed. The complexity of the calculations dictates that for reasons of practicality the D.C.F. calculations have been undertaken on a micro computer. The calculations have been undertaken by Mr. Williams with appraisal input and review being provided by myself.
>
> The actual value inclusive on non-real estate items and properties assessed on a separate folio is $341 million.

The adjusted purchase price, i.e., purchase price of $565 million, less working capital, is $485 million. The adjusted purchase price of the lands on the basis of the relationship of those lands to the total book value for the company is $295 million (exhibit 15 - page 5). By deducting the value of a marketing contract and adding back in the value of tax shields available to Elk Falls of $20 million, one arrives at a final conclusion of $285 million.

At pages 427 and following the chairman engaged in a colloquy with the witness, the upshot of which was that the witness agreed that purchasers, as far as he knew in the market place, did not address themselves directly to interest during construction, excess operating costs and external obsolescence. The point being made by the witness, although the chairman appears to have overlooked it, was that these will all be elements that a purchaser would consider when he thought about the cash flow which was what he would be most interested in.

*The Case for the Respondent*

> (a) Larry Earl Quayle, Deputy Assessor for the Courtenay Assessment Area and a member of the Appraisal Institute of Canada gave evidence on the 6th and 7th June, the 12th June and the 13th June, 1985. The actual value of the mill, calculated on a replacement cost approach, is $487,756,850.00 (exhibit 4 - page 1). The sale was not considered in the cost approach (page 583). An allowance was made for after tax excess operating costs (incurable obsolescence) of $61,134,000.00 and an economic allowance of 8 per cent on the valuation of the pulp mill and 10 per cent on the saw and planer mill as these were consistent with allowances made to other plants in the Courtenay Assessment Area because of the recession. Interest during construction was added in.
>
> At page 608:
>
> Q. What influence does the income earning capabilities of this property have on your valuation by the cost approach?
>
> A. By the cost approach - has very little, if any.
>
> Q. Is there any market evidence, to support the assumption which is inherent in your cost approach, that someone would pay the value so determined?

A. Well, I think that the - what one does in the cost approach is attempt to - you know, consider all forms of depreciation, and - in that respect, - it is done, done correctly - I would say it is a consideration, yes. Um - I think the - in the case of the subject plant, the purchase that we were discussing the statement has been made that they, you know, paid, paid book value for the - for the plant. So, I don't know. I would have to - have to say that if, you know, if - if you do it carefully, if you are conservative in your estimates of costs that you - you can approach it, that's what I've attempted to do.

Q. There's no - I put it to you, there's no market evidence whatever that anyone would pay the amount that you determine by the cost approach to be the value of this plant.

A. Yeah, there - there - there is not as comparative sale.

Q. But, - worse than that, from your point of view there is no evidence at all, is there?

A. There is no market evidence.

Q. What kind of evidence is there?

A. There is the - there is no - no market evidence I agree, - in respect to the, to the costs I think one has to, you know, consider utility. Urn - I'd have to agree there is no, no specific evidence related to this plant.

(b) Thomas Johnstone: Director of Appraisal Services to the British Columbia Assessment Authority. Interest during construction should be added in determining value by the cost approach. The principle of substitution is basic to the cost approach. That approach is based on the premise that cost equals value and if it is found at the end of the exercise that that is not so a correction can be made within the cost approach. Page 821, Volume VII:

Q. You made the comment that you could not use the cost approach if no one would replace, consider replacing the subject and you also made a comment concerning, I would say, the versatility of the cost approach. Could you explain those two remarks?

A. If there, if you had a plant scheduled for shutdown 6 months from now, one would not use the cost approach to value. One would abandon that approach altogether. If you are, you know, if you would not replace a plant in its present form or if, in fact, at this point in time it could be established that no one would ever build a pulpmill again, why would you bother with substitution? You would be looking at, you'd be saying there will never be a substitute because no one will ever do it. If that is the case in British Columbia, that there will never be another pulp and paper plant built, then I leave you with the problem of how you're going to value and I'm not sure that the cost approach will tell you that unless you make some very, very deep allowances for external obsolescence which could be the only factor that would lead you to that conclusion, that the making of pulp and paper is not now and never will be economical and no one would ever replace that production.

Mr. Savage: Thank you.

The Chairman: Nothing. Thank you very much Mr. Johnstone.

(c) Donald Richard Taylor: Area Assessor of the Courtenay Assessment Area. Exhibit 26 is his critique of market value. The value paid by Fletcher Challenge was less than it would be in a buoyant economy (page 846). Fletcher Challenge got the shares for less than their fair market value. An allowance should be made for external obsolescence because of the market down turn (page 874). As to the use of the cost approach:

Mr. Brothers: Didn't Mr. Quayle value this property using the cost approach?

A. Yes, he did.

Mr. Brothers: Has that got anything to do with the market?

A. The cost approach?

Mr. Brothers: Yes.

A. -only from the point of view that a prudent purchaser will not pay many [sic] more than what it would cost him to build an equivalent type of property or building.

Mr. Brothers: What's that got to do with the market?
A. Well, in the purest sense, cost approach in itself does not relate to market although in determining the cost approach and in considering, there are some considerations that are given to the market. As an example, we do on some properties measure the depreciation. Find that in the market place. And external allowance for economics, that could perhaps be measure [sic] also in the market place and recognized in the cost approach.

(d) Frank Slavik: Industrial Appraiser employed by the British Columbia Assessment Authority from 1979, investigated the cost of the Northwood Pulp and Paper project and assisted Quayle in the cost appraisal done by him.

(e) Ernest Mitchell: Executive Vice-President of Crown Zellerbach Corporation. His evidence goes to the question of whether the sale of the shares was a market sale. It is not relevant to the proceedings in the stated case.

(f) John Hubert Stanhope: Appraiser with the British Columbia Assessment Authority, gave a critique of the discounted cash flow method in exhibit 28:

The valuation attempted by Mr. Williams utilizing the D.C.F. technique and required rate of return (or hurdle rate) considers value only from the purchasers or Crown Forest standpoint. This technique is best suited to investment analysis or feasibility studies and is most often used for the ranking of various investment alternatives. Mr. Williams did not consider value from the standpoint of the vendor who may not wish to sell at the required rate of return utilized.

Financial analysts, accountants and engineers use D.C.F. to do two things:

1. To compare the relative worth of investment opportunities when available funds require that one make a choice.

2. To estimate whether a particular proposed investment is likely to yield a return on capital invested, which meets some internal criterion of the investor or required rate of return.

The D.C.F. analysis then simply helps the investor to decide whether that value is satisfactory for him. Since we are looking solely at an investor's viewpoint, we do not see any guide to the vendor's position.

Apart from the above observations, the D.C.F. approach has other weaknesses as a method for valuation. The first is that it depends totally on a set of assumptions far into the future, which assumptions may prove to be totally incorrect as time passes and which are unlikely to be universally agreed upon. The second defect, which is linked to the first is that the method is very sensitive to any changes in those assumptions such as

exchange rates, labour rates, energy costs, wood costs, product prices, operating levels, etc.

For these reasons the D.C.F. method should not be relied upon to produce an estimate of value for assessment purposes. For comparing different investments, it may well be a useful tool, since the accuracy of assumptions about the future is less important than the fact that one uses the same assumptions for both competing investments. The method ranks investments in order of desirability, but does not tell us what either investment is worth in absolute terms.

As an appraiser for assessment purposes I am precluded from using the D.C.F. technique as it is based almost totally on hypothesis.

As a result of the sensitivity of the projections of the D.C.F. analysis and the great number of hypotheses running for 20 years or almost 4 business cycles according to Dr. Styan, I would prefer to put much more reliance on other approaches to value normally used for this type of property such as the Cost Approach.

As a backup to the Cost Approach a stabilized net operating income based on averaging several years experience could be capitalized at a rate commensurate with the security and durability of the income stream.

Using a stabilized net operating income before tax and depreciation taken over a period of years will tend to average out irregularities and take into consideration fluctuations in the business cycle. This is a method commonly used by most real estate appraisers on major income producing properties.

The mill can be valued on a capitalized income stream. His analysis is based on two numbers and the entire result depends on the validity of the capitalization rate and the stabilized earnings rate (page 45-28th June, 1985).

(g) William Payne: partner in Touche Ross and Company, allocated the purchase price of the shares by exhibit 31:

. . . on the premise that assets are worth what they can earn, [there should be] an asset allocation to the Elk Falls component of the company as a whole of 82.34% with no inflation adjustment and 80.05% after inflation adjustment.

Because Fletcher Challenge Ltd., in doing its own corporate returns, indicated that it put an additional value of $172 million on the acquisition, the value of Elk Falls was $575 million by Fletcher Challenge's own figures and $435 million from the actual price paid (schedule 3, exhibit 31). In doing his allocation he did not take into account that certain of the production and earnings of the pulp and paper division come from plants on the Mainland nor did he take into account that the saw mill on the lands being valued, which is part of the wood division, was losing money.

THE LAW
By section 26:

PART 3

VALUATION

Valuation for purposes of assessment

26. (1) In this section

"actual value" means the actual value that land and improvements would have had on July 1 had they and all other land and improvements been on July 1 in the state and condition that they are in on September 30 and had their use and permitted use been on July 1 the same as they are on September 30;

"September 30" and "July 1" mean

(a) in relation to an assessment roll completed as required by section 2 (1), September 30 and July 1 of the year during which the assessment roll is completed, and

(b) in relation to a revised assessment roll completed as required by section 2 (1.1), September 30 of the year during which the revised assessment roll is completed, and July 1 of the year immediately before that.

(2) The assessor shall determine the actual value of land and improvements and shall enter the actual value of the land and improvements in the assessment roll.

(3) In determining actual value, the assessor may give consideration to present use, location, original cost, replacement cost, revenue or rental value, market value of the land and improvements and comparable land and improvements, economic and functional obsolescence and any other circumstances affecting the value of the land and improvements.

(3.1) Without limiting the application of subsections (1) to (3), where an industrial or commercial undertaking, a business or a public utility enterprise is carried on, the land and improvements used by it shall be valued as the property of a going concern.

I contrast this section with sections considered in some other assessment cases:

(a) By the Court of Appeal of Saskatchewan in *City Savings and Trust Co.* v. *City of Regina* (1974) 52 D.L.R. (3d) 698 at 701:

14. In determining fair value for any of the purposes of this section or any other section of this Act the assessor may take into consideration and be guided by any applicable formula, rule or principle set forth in a manual prepared for the guidance of assessors and approved by the minister.

The Court said:

At all pertinent times all buildings in the Province were assessed upon a replacement cost basis. A manual prepared by the Department of Municipal Affairs and approved by the Minister sets forth that assessment be made on a percentage of the replacement cost of buildings; that an allowance may be made for functional obsolescence; and that no assessment take into consideration the financial return from the property.

City Savings and Trust Company appealed the assessment to the Saskatchewan Assessment Commission contending that the building should have been assessed upon its market value which is determined not on a cost basis but upon its financial performance. The market value, says the appellant, is directly dependent upon the net yield to be anticipated by a prospective purchaser.

The Court held that as the statute provided that the manual be used, the taxpayer could not complain that the assessor had given no consideration to the revenue from the building.

(b) By the British Columbia Court of Appeal in *Bishop of Victoria* v. *City of Victoria* [1933] 4 D.L.R. 524 at 526:

It may be mentioned, however, that the law respecting valuation of property for assessment purposes has been frequently changed by the Legislature in past years. In 1914 the law gave directions as to how the value for assessment purposes should be found in these words:-

"For the purpose of taxation, land and improvements shall be estimated at their value, the measure of which as to land shall be the actual cash value, and as to improvements shall be the cost of placing at the time of assessment such improvements on the land, having regard to their then condition, but land and improvements shall be assessed separately:" (*Municipal Act*, 1914 (B.C.), c. 52, s. 199).

This may be called the replacement value. Earlier the statute read as follows:

"For the purposes of taxation, land and improvements within a municipality shall be estimated at their value, the measure of which value shall be their actual cash value as they would be appraised in payment of a just debt from a solvent debtor; but land and improvements shall be assessed separately:" (*Municipal Clauses Act*, 1896 (B.C.), c. 37, s. 112).

Finally by s. 212 (1) of the *Municipal Act*, R.S.B.C. 1924, c. 179:-

"For the purposes of taxation, land, except as hereinafter provided, shall be assessed at its actual value, and improvements shall be assessed for the amount of the difference between the actual value of the whole property and the actual value of the land if there were no improvements: Provided, however, that land and improvements shall be assessed separately."

The effect of this statute is to direct the assessment of the building in question at the "actual value."

(c) By the Privy Council in *City of Montreal* v. *Sun Life Assurance Company* [1952] 2 D.L.R. 81 at 89:

The ascertainment of the amount of the assessment is entrusted to assessors and ss. 373 and 374 of the Charter contain provisions as to their appointment and constitution. The statement of their duties begins with s. 375 [am. 1941 (Que.), c. 73, s. 33] which enacts:-

"375 (a) Every three years the assessors shall draw up in duplicate for each ward of the city a new valuation roll for all the immoveables in such ward. Such roll shall be completed and deposited on or before the first of December, after having been signed by the chief assessor.

"This roll . . . shall contain

"(3) The actual value of the immoveables."

The French text uses the phrase "valeur reelle" but it is common ground that both expressions bear the same meaning.

(d) By the Supreme Court of Canada in *Grierson* v. *City of Edmonton* (1917) 58 S.C.R. 13 at 16:

Section 321 of the charter of the city of Edmonton is as follows:-

> Land shall be assessed at its fair actual value. In estimating its value regard shall be had to its situation and the purpose for which it is used or if sold by the present owner it could and would probably be used in the next succeeding twelve months. In case the value at which any specified land has been assessed appears to be more or less than its true value the amount of the assessment shall nevertheless not be varied on appeal, unless the difference be gross, if the value at which it is assessed bears a fair and just proportion to the value at which lands in the immediate vicinity of the land in question are assessed.

(e) By the Nova Scotia Supreme Court in *Mersey Paper Co. Ltd.* v. *County of Queens* (1959) 18 D.L.R. (2d) 19:

> All property liable to taxation shall be assessed at its actual cash value, such value being the amount which in the opinion of the assessor it would realize in cash if offered at auction after reasonable notice but in forming such opinion the assessor shall have regard to the assessment of other properties in the town or municipality so as to ensure that taxation shall fall in a uniform manner upon all real property in the town or municipality and that taxation shall fall in a uniform manner upon all personal property in the town or municipality.

*Assessment Act* R.S.N.S. 1954 c. 15 R. 2.

Thus, in Saskatchewan, statutory approval was given to the use of appraisal principles; in British Columbia, in 1914 "replacement" (i.e., reproduction cost) was the measure for valuing improvements; in the City of Montreal the test was simply "actual value" without any statutory criteria and in Nova Scotia it was the value which, in the opinion of the assessor, the property would realise in cash if offered at auction.

Under the British Columbia statute, this Court has no power to substitute its opinion on questions of fact for those of the Board.

So long as the Assessment Appeal Board which must, in deciding appeals to it, apply the Act does not:

> 1. misinterpret or misapply the section-see *Pacific Logging Co. Ltd.* v. *The Assessor* [1977] 2. S.C.R. 623 adopting the dissenting judgment of McIntyre, J.A. in the Court of Appeal 12th November, 1976 (unreported);
>
> 2. misapply any applicable principle of general law (a concept relevant only to one of the questions in the stated case), or
>
> 3. act without any evidence or upon a view of the facts which could not reasonably be entertained this Court has no power to intervene.

On the third proposition, which is fundamental to the appellant's case, see:

(a) *Edwards* v. *Bairstow* [1956] A.C. 14 (H.L.) at 29:

> For it is universally conceded that, though it is a pure finding of fact, it may be set aside on grounds which have been stated in various ways but are, I think, fairly summarized by saying that the court should take the course if it appears that the commissioners <u>have acted without any evidence or upon a view of the facts which could not reasonably be entertained</u>.
> (Underlining mine).

(b) *Provincial Assessors of Comox, Cowichan and Nanaimo* v. *Crown Zellerbach Canada Ltd. et al* (1963) 42 W.W.R. 449 at 458:

> But that is really beside the point, because neither this court nor the court below has any right to make findings of fact on the evidence before the board; that was the function of the board, and its findings of fact are set out in the stated case as the foundation for the questions of law that are asked, and we must accept those findings as the case does not raise any question of absence of evidence to support them.
> (Underlining mine).

(c) *Swan Valley Foods Ltd.* v. *Assessment Appeal Board* (1979) 13 B.C.L.R. 304 (B.C.S.C.) affirmed (1980) B.C.L.R. 358 (B.C.C.A.) at 362:

> "The petitioner appealed to this court by way of stated case. The court was asked whether the board was correct in deciding that the replacement-cost method of determining actual value was the only proper method of assessment. I held, on what I considered to be the authority of *York Assessment Office Assessment Commr.* v. *Office Specialty Ltd.*, [1975] 1 S.C.R. 677, 49 D.L.R. (3d) 471, 2 N.R. 612, that it was not. I conceived that the case stood for the proposition that where the assessor is in search of an 'actual' or 'market' value, he may use replacement-cost as a yard stick but only where he can regard the owner as a possible purchaser and then only to such amount as the owner would be willing to pay to replace that which is valued. In the present case there is no evidence that the owner would be willing to pay the replacement-cost. All evidence is to the contrary."
>
> As I understand counsel for the appellant, he does not disagree with the proposition of law as stated in that passage, but, it is his contention that on the evidence the learned trial judge was in error in holding that the owner would not be willing to pay the replacement-cost.
>
> I have recited the circumstances lying behind this appeal in considerable detail because those circumstances indicate to me that the learned chambers judge was correct. I have reached the conclusion he reached, that in the present case there was no evidence that the owner would be willing to pay the replacement cost. Having reached that conclusion, I would dismiss the appeal. .
> (Underlining mine).

The third proposition enunciated will avail the appellants not at all if the *Assessment Act* means that the Board may value on replacement cost whether or not there is evidence warranting such a method. It is open to the Legislature to do as was done in Saskatchewan. I do not, however, think it has done so for these reasons:

(a) the term "replacement cost" in section 26 is not used as a term of the contemporary appraisers' art. It first made its appearance in the Statutes of British Columbia in 1948 in the *Municipal Act Amendment Act* S.B.C. 1948 c. 61 s. 11 and I have been around long enough to know that at that time the term commonly meant what appraisers now mean, thirty-seven years later, by reproduction cost and see the use by Macdonald, C.J.B.C. of the term "replacement value" in the *Bishop of Victoria* case (supra) at page 526;

(b) the words "may give consideration to" do not warrant the adoption of a method without evidence that a purchaser or owner would use that as a means of determining what he would pay for the lands. To put it another way, the words do not empower the Board to act in breach of the third proposition. This interpretation of section 26 is implicitly adopted in the *Swan Valley* case.

Having read all the evidence, I was struck by, to me, a singular omission-not one of the witnesses gave any weight in computing the actual value of the lands to the contribution made by the work force to the earning ability of Elk Falls. The value of their contribution is not subject to assessment. Without a competent existing work force from the manager down to the lowliest labourer, would Fletcher Challenge have paid what it did for the shares? Perhaps-but only if in our depressed economy they could easily gather up such a work force. The proposition seems to be in the discounted cash flow analysis, the income capitalization method and the allocation of share purchase price by income stream that it is the land and the machinery which produces the earnings and people have nothing to do with it. This may be classic capitalist theory but strikes me as absurd. As it is patently obvious, however, that all the witnesses accepted this view without argument I say no more about it.

I was struck also by something else: the absence of any evidence that any purchaser of any industrial complex, let alone a purchaser of a pulp mill, would have considered in 1982 the replacement cost in the way that the theorists put it forward in determining what he was prepared to pay. That business assets are worth what they can earn when they have no higher or better use, either separately or as an integrated whole, I consider to be self evident. When I say "what they can earn" I am not saying that there are not many acceptable ways of using that self evident proposition to arrive at actual value of income producing lands. Every method of computing a value from earnings is subject to error-it must, of necessity, give a present value to future expectations. The seductive charm of the cost approach is in its not concerning itself with present expectations of the future, but I do not consider any reasonable man could entertain it as a method of determining actual value of this complex.

The cost approach is nothing more than a theory without any evidentiary foundation. If, however, it is open to this tribunal to use this theory, then I fail to see how it can use it in part and reject the rest of it.

Having tentatively come to the conclusion that the Board's use of the cost approach was unwarranted by the evidence, I sent to counsel a memorandum:

> I am *tentatively* of the opinion that the use by the Assessment Appeal Board of the cost approach was without any proper foundation for these reasons:
>
> 1. The cost approach is based on the principle of substitution.
>
> 2. There is no evidence that purchasers generally, or purchasers of pulp mills in particular, act on any such principle; in other words, it is a mere hypothesis of theory of behaviour.
>
> 3. In the absence of evidence, that in the market place purchasers do behave in that way, there is no evidentiary foundation for the principle unless the Board was entitled to take some sort of judicial notice or the Board is authorized by s. 26 to use this approach whether or not there is evidence of behaviour in the market place.
>
> 4. The use of comparables in valuation is founded on judicial notice, i.e. it is notorious that people buy and sell according to what similar goods or realty are fetching in the market place.
>
> 5. The Board rejected interest during construction and excess operating costs on the grounds that there was no evidence that purchasers in the market place pay attention to these matters but nonetheless adopted the principle of substitution itself for which there was equally no evidentiary foundation.
>
> 6. While s. 26 says the tribunal may consider "replacement costs", there is no reason to conclude that by using that term, the legislature intended to authorize the Board to use the principle of substitution without an evidentiary foundation.

I should like counsel to address themselves to these questions:

1. Is it open to the Board as a matter of law to adopt the cost approach in the absence of any evidence that the principle of substitution is other than a theory or hypothesis?

2. Does s. 26 of the Act authorize the Board to apply the principle of substitution in the absence of evidence that purchasers generally or purchasers of pulp mills in particular (whether the purchase is direct, i.e. of the lands, or indirect, i.e. by buying the shares of a company that owns the pulp mill), make their decisions on the basis of substitution?

3. Is it reasonable for the tribunal if it is open to it in this case to adopt the principle of substitution without any evidence that the principle is one applied in the market place, to then reject, on the grounds of lack of evidence, other parts of this appraisal theory?

4. If the evidence of Mr. Ryan is that earnings were the dominant consideration in the decision to buy, and as there was other evidence that earnings were a dominant consideration in investment decisions in the forest industry, was the Board's decision to adopt the cost approach one a reasonable tribunal could come to?

5. Do the questions as posed permit me if the answers to any of the above four questions is "no" to express such an answer or answers or should the case be remitted to the Board for amendment? If so, should this be done before or after my reasons are delivered?

Mr. Savage responded to question 5:

The case need not be remitted to the Board for amendment. The Court can give the Board general guidance in the context of the questions posed by the Appellant and the Respondent.

Mr. Wallace answered:

The case need not be remitted to the Board for amendment. Questions 1, 2 and 4 can be answered in the context of answering questions 2(c) and 2(d) of the Stated Case stated at the request of the Appellant. Question 3 can be answered in the context of answering questions 2(e) and 2(f) of the Stated Case stated at the request of the Appellant and questions 1 and 2 stated at the request of the Respondent.

I now turn to the questions put by the appellant.

*Question 1:*

In the Board's "Final Estimate of Value" by the "Direct Sales Comparison Approach (Share Purchase Allocation)",

(a) Was there any evidence before the Board on which it could conclude that the earnings on which its allocation depended were the earnings of the assets at issue?

(b) Did the Board err in law in rejecting the Appellant's share purchase allocation based on net book value as indicating the upper limit of the actual value of the assets at issue?

*Question 1(a)* arises in this way: as I have already indicated, a difficulty arises because Mr. Payne, who gave evidence on the share purchase allocation, did not have access to all the books and records of the appellant and determined what income came from what asset by using some figures in the company's annual reports.

In the reports the income was broken down by divisions called, pulp and paper, wood products and merchandising. See, for instance, Crown Zellerbach Canada Annual Report 1982, pages 8 and 9 and Crown Zellerbach Canada Annual Report for 1981, also pages 8 and 9, both of which are part of exhibit 1. But, as was pointed out by counsel, it is almost incontrovertible on the internal evidence of these reports, e.g. the 1982 report at page 6 that for administrative purposes the earnings of the plants at Kelowna and Richmond are included under the pulp and paper division and the losses from the saw mill on the land under assessment are included under wood products' division.

I think it was unreasonable for the Board, when it was adopting Mr. Payne's method, not to deduct from the earnings of the pulp division the earnings from the Mainland plants and the losses from the saw mill. Mr. Savage, for the assessor, directed me in answer to this contention of the appellant to certain remarks made by witnesses to the effect that all the pulp and paper division was at Elk Falls. But to take these answers out of the context in which they were given and give them the meaning attributed to them by Mr. Savage is, I think, to be unfair to the witnesses and to misconstrue the answers. If a witness had been asked: into what division do the earnings of the Kelowna and Richmond plants go? and he had answered that they go into wood products or merchandising, I would agree with Mr. Savage.

Thus, the answer to question I(a) is:

> No, because there were included in determining the earnings of the subject matter of the assessment, the earnings of other lands and there were not deducted losses of the saw mill which was part of the subject matter of the assessment.

*Question 1 ( b)* arises because:

> 1. Fletcher Challenge paid net book value, plus $23 million for the shares.
>
> 2. The assets are carried at historic costs and thus those assets which were acquired a long time ago are obviously worth more than book value and those acquired recently such as the new paper machine at Elk Falls, a large component of the mill's value, are worth at most what was paid for them.

I do not think this is a question of law and, therefore, the answer to this question is, "no".

*Question 2:*

In the Board's "Final Estimate of Value" by the "Cost Approach",

> (a) Was there any evidence before the Board upon which it could conclude that the replacement cost of the assets at issue was $661,014,000?
>
> (b) Did the Board err in law in considering the Kemper Group insurance appraisal and other materials which were marked for identification but which were not introduced into evidence and upon which no opportunity was afforded the Appellant to test the correctness or applicability of their contents in cross-examination?
>
> (c) If Question 2(a) is answered in the affirmative, was there any evidence before the Board that a purchaser would pay to acquire the assets at issue, the amount the Board determined as the actual value?
>
> (d) If the answer to Question 2( c) is in the negative, did the Board err in law in relying on the Cost approach in the absence of any evidence that a purchaser would pay the amount so determined as actual value in order to acquire the assets at issue?

(e) If Question 2(d) is answered in the negative, did the Board err in law in refusing to deduct in its calculation of actual value an amount for functional obsolescence due to ongoing excess operating costs?

(f) If the answer to Question 2(d) is in the negative, did the Board err in law in refusing to deduct in its calculation of actual value an amount for external obsolescence?

(g) If the answer to Question 2(d) is in the negative, was the Board's conclusion that the "No. 5 paper machine and ancillary expansion" had an undepreciated assessable value of $190,000,000.00 contrary to all the evidence and therefore an error in law?

As to question 2(a), the answers proposed by the parties are:

Appellant's answer:

No. There is no evidence before the Board upon which it could arrive at any conclusion with respect to the replacement cost of the assets at issue; its determination of actual value by the Cost Approach is, therefore wrong in law.

Respondent's answer:

No; $661,014,000 is replacement cost minus interest during construction. There is also a mathematical error in the Board's calculation.

What underlies the appellant's proposed answer is its submission that in arriving at the replacement cost the assessor relied on, and the Board must have accepted, inadmissible evidence, namely, the documents and other evidence referred to in question 2(b). For the reasons which I have given in answering question 2(b) I do not consider the appellant can sustain that objection.

What underlies the respondent's answer is that it submits that there must be added to other costs of replacement "interest during construction" whether or not the owner is going to build with borrowed money or with its own resources.

There was evidence from one of the witnesses for the appellant that to build the mill might cost $500 million to $600 million and might go as high as $800 million and, from a witness for the respondent that the cost of construction of a replacement mill would be approximately $661 million. I do not see, therefore, how it can be said that there was no evidence upon which the Board could conclude that replacement cost was $661 million. That, of course, is not to say that that figure represents "actual value" or that that figure should be used as a basis upon which to calculate physical depreciation and, thereafter, actual value.

In my opinion, therefore, the answer to this question is "yes".

*Question 2(b)* arises because the Board used as a foundation for determining replacement cost various documents marked A, B, C and D for identification when the authors of the documents were not called to give evidence. I do not think the Assessment Appeal Board is bound by the strict rules of evidence. Its proceedings can only be vitiated by a non-adherence to the rules of evidence if such non-adherence leads to a breach of natural justice. I cannot see that there was any failure of fundamental fairness in the use of the documents in issue.

Thus, my answer to this question is, "no".

Questions 2(c) and (d) raise, albeit awkwardly, the issue of using the cost approach in this case. It is clear Mr. Savage so understood question 2(c) for his proposed answer to it is "Yes, the replacement cost approach is available."

I have already indicated my doubts about the use of this method in this case.

Mr. Savage urges upon me the decision of the Supreme Court of Canada in *The Assessment Commissioner of York Assessment Office* v. *Office Specialty Ltd.* (1975) 49 D.L.R. (3d) 471 in which Judson, J. said for the Court at 475:

> How does an assessor determine "actual" or "market" value on facts such as we have in the present case? This is a modern, standard, one-storey building, badly located for a general purchaser but entirely suitable and satisfactory to its owner. It is not for sale and it is not likely that it will be offered for sale. I think that in ascertaining "actual" or "market" value, an assessor has to regard the owner as a possible purchaser or estimate what he would expend on a building to replace that which is being valued.
>
> The principle is well stated in *Montreal* v. *Sun Life Assurance Co. of Canada*, (1952) 2 D.L.R. 81 at p. 90 in these terms:
>
> Their Lordships would agree that where no sale is contemplated and indeed any sale would be difficult what has been called the higgling of the market is not an element of much if any consequence, but nevertheless the ultimate aim is to find the exchange value of the property, i.e., the price at which the property is salable. In reaching their result the appointed Tribunal must take into account not only the amount which a buyer would give but also the sum at which the owner would sell. What that sum would be is, as the authorities have pointed out, best ascertained either by regarding him as one of the possible purchasers or by estimating what he would be willing to expend on a building to replace that which is being valued. But the owner must be regarded like any other purchaser and the price he would give calculated not upon any subjective value to him but upon ordinary principles, i.e., what he would be prepared to pay, if he was entering the market, for a building to meet his requirements, or would be willing to expend in erecting a building in place of that which is being assessed.

But in neither the *Sun Life* case nor the *Office Specialty* case was there, as there is in this case, evidence of a recent sale even though it is a sale of the shares of the owner and not of the lands and evidence of the use by the owner of the income stream to determine value and no evidence, to use the words of Meredith, J. in the *Swan Valley* case quoted by Hinkson, J.A. at page 362 "that the owner would be willing to pay the replacement cost".

I find it difficult to accept that if the shareholders of *Office Specialty Ltd.* had, shortly before their case began, sold all the shares in that company to a new owner the Supreme Court would have had the same view of the applicability of the cost approach.

On the basis that what the appellant is really asking and what the respondent understood the appellant to be asking by this question, is whether a reasonable tribunal could, on the evidence in this case, use the cost approach to determine actual value within the meaning of section 26, my answer to question 2(c) is "no" for the reasons which I have attempted to express at pp. 26-28 of this judgment.

As to question 2(d), I do not see the point of the words "if the answer to question 2(c) is in the negative. . .". To my mind this question is simply question 2(c) posed in a different way. For the reasons which I have given as to why the cost approach should not have been used on the evidence in this case, my answer to this question is "yes".

The remaining parts of question 2 begin with the words "if question 2(d) is answered in the negative". As I have answered question 2(d) in the affirmative, I am not required by the stated case to answer these questions and I do not do so.

I note, however, that the respondent's proposed answers to these questions are:

> 2(e) Yes, the Board's finding is contrary to all the evidence, but the amount is a matter for the Assessment Appeal Board. The Board's reasoning is in error.
>
> (f) Yes, the Board's finding is contrary to all the evidence, but the amount is a matter for the Assessment Appeal Board. The Board's reasoning is in error.
>
> (g) No.

As to (e) and (f), these are the matters which Macdonald, J. referred to as matters of appraisal principle and, therefore, of law. I agree with the respondent's answers to (e) and (f) but not for the same reason as Macdonald, J. I simply say that if a tribunal is going to use an hypothesis or theory developed in a branch of science or art and for which there is no evidentiary foundation, it must take the theory whole or not at all. To do otherwise is to come to a determination no reasonable man could come to. It is not reasonable for the Board to adopt the principle of substitution without evidence that it even exists in the minds of purchasers of lands such as these and then reject other parts of the theory on the ground that there is no market evidence to support their validity.

*Question 3:*

With respect to the Board's rejection of the "Income Approach (Discounted Cash Flow Analysis)" ("DCF"),

> (a) Was there any evidence before the Board upon which it could conclude that in the Appellant's DCF analysis "the capital investment base for the asset value was the book value"?
>
> (b) Did the Board err in law in its conclusion that because, "'Forecasts are never a fact', . . . discounted cash flow analysis is not an appropriate method to determine actual value"?
>
> (c) Did the Board err in law in its conclusion that DCF analysis cannot be used to "value the property as it stands at the date of assessment"?
>
> (d) Was the Board's conclusion that the rate of return in the Appellant's DCF analysis is "not founded on fact that the market place would sustain such rate" contrary to all the evidence?

I think the whole question might simply be put in this way: was it an error in law for the Board to reject the income approach (discounted cash flow analysis) as a method for determining the actual value of the lands? It can only be so if it acted:

> (a) without any evidence; or
>
> (b) upon a view of the facts which could not reasonably be entertained; or, perhaps
>
> (c) if it rejected the method because some one or more of its reasons was founded on a view of part of the evidence which no reasonable man could entertain even though other of its reasons were founded on a view of other parts of the evidence which a reasonable man could entertain.

The Board rejected the method saying:

> Counsel for the appellant referred to the case of *Courtot Investments Limited* v. *Royal Trust Company* (Supreme Court of Ontario-August 28, 1980) in support of the appropriateness of the discounted cash flow analysis. It is noted that that case involved a contract between the parties which required the future values of lease incomes to be determined. The trial judge found the method to be appropriate in determining the probable future worth of the contract. Valuation for assessment is quite another matter. There are countless cases which enunciate the principle that the assessor must value the property as it stands at the date of assessment. Future values have no place in assessment valuation; those values are the subject of future assessments.

The first error made by the Board is in its rejection of the judgment in the *Courtot* case. This paragraph simply mis-states both the issue of law before Boland, J. in that case and the judge's decision. In that case, the judge had first to determine the value of a building at a date in the past if the defendant had performed its contractual obligation to the plaintiff found to exist in these words:

> The Royal Trust Company in return for these exclusive lease rights will guarantee the leasing minimum of 100,000 sq. ft. of space in the Courtot Centre for a period of eighteen months.

The Royal Trust Company did not effect such leases and the plaintiff lost its building on a distress sale. So the first question was what would the building have been worth on the date of the distress sale with the leases in place and, the second question, how much of the difference between that notional value and the sale price was the result of the breach and how much the result of the distress sale? The reason why the plaintiff did not get all the difference is explained on page 37 of the judgment.

Thus, the learned judge was valuing the property as of the date of the sale. I can see no difference in what she was doing and what the law requires the Board to do. The judge was not determining the value at some future date, nor was she taking into account events after the relevant date.

The second error is in the words "future values have no place in assessment valuation" if they mean the Board cannot give a present value to an expected future benefit. If, however, they mean that the Board cannot look at events occurring after the relevant date, i.e., a sale of land occurring six months after the assessment date as a comparable, they are probably right, although even this proposition must not be taken too far. I see no reason why, in common sense or law, evidence of events occurring after the appropriate date should not be used to test the validity of the forecasts and assumptions of experts as was done by Fulton, J. in *Diligenti* v. *R.W.M.D. Operations Kelowna Ltd.* (1977) 4 B.C.L.R. 134 at 142. By such means one is testing the wisdom of the experts. *Diligenti* was, of course, a case on the fair value of shares bought pursuant to the oppression provision for the *Company Act*. However, I do not consider that the law should be divided into water tight compartments and the approach to evidentiary questions, whether the valuation is one of land under assessment provisions or shares under dissent provisions should, subject always, of course, to the overriding words of the applicable statute, be approached in the same way.

As the Board misconstrued the judgment in the *Courtot* case, I consider the whole paragraph is an error in law.

But the Board is right when it says that DCF analysis assumes "future sales, costs, exchange rates and other extremely sensitive factors which are, at best, predictions". Indeed, the method appears to me from its description to be so complex that unless the modern computer had been invented this method could not have been invented either. Boland, J. describes the discounted

cash flow analysis method in her judgment in the *Courtot* case and it accords with the understanding of it given to me by the evidence in this case. If the Board had rejected this approach as something new and untried that might be within its rights. I say, "might" because the evidence was that this new method was in use within the industry for the purpose of making investment decisions and if a method is in use generally, then it should not be rejected out of hand as a method of determining actual value. It would be just as unreasonable to do so as it would be to reject the computer as a method of assisting in analyses generally.

Discounted cash flow analysis is not without its pitfalls as illustrated by the series of judgments delivered by My Lord the Chief Justice in *Cypress Anvil Mining Corporation* v. *Dickson and Others* Vancouver Registry C792523, 21st October, 1982, 40 B.C.L.R. 180, 27th January, 1983 and 22nd May, 1984, where the result of the first calculation done was to give a value of between $18.00 and $22.00 a share when the offering price, which had been arrived at in negotiations between two hard-headed business men, was $1.50 per share.

The Board also said:

> With respect to the future business of the company and the forecast of which the discounted cash flow analysis is only one of several scenarios considered, Mr. Ryan made a most frank statement - "forecasts never are a fact, are they!"

It is, of course, true that forecasts never are a fact unless and until the forecast event occurs. Nonetheless, all transactions of purchase and sale either directly or indirectly of income producing properties must have in them an element of forecast. Earnings projections are the very stuff of actual value.

This method of determining actual value is open to the Board under section 26 (2) of the Act and I consider it was an error in law for it to reject this method for the reasons it gave. I am not, however, saying that if, upon further consideration, the Board rejected the method for other reasons it would necessarily be committing an error in law. The Board is not bound to accept the discounted cash flow analysis method or the result arrived at by it in this case.

I think, therefore, that I should answer questions 3 (b) and (c) "yes" and not answer questions (a) and (d) which are not really the thrust of the appellant's case.

> *Question 4*: Did the Board err in law in not concluding that the value of the Elk Falls Industrial Complex as a business sets the upper limit of the actual value pursuant to section 26 of the Act, of the assets at issue?

My answer to this question is "yes". I do not see how any reasonable man could hold that the market value of the land exceeded the value of the complex as a business or going concern, including the lands within the assets of the business. In the absence of any evidence that the lands had some special value apart from the business, e.g. if oil or gold had been discovered under them or the land was something that could reasonably be lived off. There are from time to time examples in the business world of that happening. By way of illustration, from a matter recently before the Court, the shares of Woodward Stores Ltd., a Vancouver merchandising company, were valued in the market and trading on the Toronto Stock Exchange until recently at $11.00 per share. Then an offer was made to the shareholders of $19.00 per share, the offeror having the intention to live off the lands and dispose of the merchandising business. There is, however, in this case not the slightest shred of evidence that the land with its installations upon it, can or might possibly fetch in the market place more than the business value of the going concern.

> *Question 5*: Did the Board err in law in refusing to allow the Appellant to call evidence in rebuttal relating to the issue of the appropriate allocation of the price paid for the shares of Crown Zellerbach Canada Limited?

This question arises in this way: at the end of the assessor's case the respondent desired to call evidence to show, by way of disputing the share allocation done by Mr. Payne, that all the assessments of all the assessable interests owned by the appellant other than Elk Falls added to the Elk Falls' allocation done by the assessor exceeded the total purchase price. This matter is dealt with at page 197 and following of the proceedings on the 29th June, 1984.

The counsel for the appellant put his position thus:

> The allocation has been made that all of the properties of this company are worth $512 million and that almost all of them, and in one analysis using Mr. Payne's numbers, more than all of that amount is attributable to the Elk Falls mill and I am submitting this exhibit to simply show what, the magnitude of other assessable assets of this company are, all of which must have an allocation of the work done by Mr. Payne and Mr. Stanhope.

The chairman ruled thus at page 199:

> In considering the proposition the Board finds that this evidence is new evidence not adduced through the defendant's witnesses and therefore is a classic example of the appellant splitting his case and, therefore, the evidence is inadmissible at this time,. Inadmissible.

I take the law to be that a tribunal has a discretion whether to admit rebuttal evidence even if that evidence is confirmatory. See *Mersey Paper Co. Ltd.* v. *The County of Queens* (1959) 18 D.L.R. (2d) 19 at 37 (NSSC) and the authorities therein cited. The term "splitting one's case" while it has a dramatic ring, means no more than the evidence is confirmatory. The Board's ruling is put in such terms that I can only conclude it did not think it had a discretion. I take it also to be clear law that if a tribunal denies the existence of a discretion when it has in law a discretion, that denial is itself an error in law.

From the transcript it does not appear that any authorities were cited to the Board on this point and as the point is a difficult one, one cannot fault the Board for not acceding to the appellant's submission. Thus, while I think the answer to this question is "yes" there must be added to it this "the Board has a discretion whether to admit such evidence and should direct its mind to the question of whether that discretion should or should not be exercised in favour of the appellant".

*Questions Stated at the Requirement of the Assessor of Area 06-Courtenay:*

*Question 1:*

> Did the Assessment Appeal Board err in law in failing to include in the Cost Approach an allowance for interest during construction when all of the evidence before the Board supported the making of some allowance?

*Question 2:*

Did the Assessment Appeal Board err in law in finding that the method of calculating interest during construction by the Assessor contemplates a future worth of monies, and therefore, is not a proper method to determine value for assessment purposes?

These questions are founded upon the cost approach hypothesis. For reasons which I gave in commenting on questions 2 (e) and (f), I do not think it was reasonable of the Board to reject the notion of "interest during construction" on the ground there was no market evidence to support it. Thus, if the cost approach is to be used at all, the answer to the question must be "yes" , but as I do not think the cost approach should have been used, I think the appropriate answer to the question is "if the cost approach was open to the Board, it erred in law in failing to include an

allowance for interest during construction". I comment also that the "evidence" referred to in the question was evidence of the theory, not evidence of behaviour, in the market place.

Question 2, which is founded upon the same supposition as the first question, i.e., that the cost approach was a proper one, should be answered similarly. My answer to that question is "if the cost approach was open to the Board, it erred in law in finding that the method of calculating interest during construction, because it contemplated a future worth of monies, was not a proper method to determine value ".

As to what should be done, I gratefully adopt the last paragraph of the judgment of McKay, J. in his judgment referred to at the beginning of these reasons:

> I am unaware of the procedures adopted by assessment appeal boards in cases where the opinion of the court is that there has been a number of errors of law-particularly, as is the case here, where the errors are such as to permeate the whole decision making process. In this case justice can only be done, short of another full hearing before a different panel, by permitting counsel to make full submissions on all aspects of the assessment. It will then be for the Board in the light of these reasons and those submissions to determine afresh the "actual value" of the Powell River mill complex.

As did McKay, J. in his case, I too, shall cause these reasons to be forwarded to the Board as the opinion of the Court.