The Implications of the Delgamuukw Decision for the Valuation of Resource Tenures in British Columbia

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Preliminary Draft: Comments Welcome

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1. *Introduction and Overview*

The decision of the Supreme Court of Canada in *Delgamuukw v. British Columbia* will have far-reaching consequences for land tenure and resource use in the Province. The *Delgamuukw* decision has pushed the definition of aboriginal title much further towards a *proprietary ownership* concept and away from the alternative *usufructuary rights* concept. It has also provided for the possibility that proof of ownership can be demonstrated by oral evidence that exclusive occupancy has occurred, on a reasonably continuous basis, since the time at which the Crown asserted sovereignty over the land. It has, therefore, very much raised the stakes in the aboriginal title settlement game, and has significantly strengthened the negotiating position of all aboriginal claimants.

Although the impact of the *Delgamuukw* decision gave further impetus to the completion of the *Nisga'a Final Agreement,* and led to the clear identification of Nisga'a Lands as lands owned in *fee simple* by the Nisga'a Nation, very little in substance has been changed from the *Nisga'a Agreement-in-Principle* by the *Delgamuukw* decision. However, the substantial transfer to the Nisga'a Nation of *fee simple* ownership of 1930 square kilometres of B.C. Crown lands and 62 square kilometres of Indian reservation lands now looks much more modest in the light of the *Delgamuukw* decision. Whereas the *Nisga'a Final Agreement* is roughly consistent (on a per capita basis) with the dedication of five percent of the B.C. land base to the aboriginal title settlement process, the claims of other First Nations involve, in total, a far larger percentage of the land base, and it is these claims that have been provided with further ammunition by the *Delgamuukw* decision. Indeed, the decision could play into the hands of those who might wish to exaggerate their claims and to pursue them by confrontational techniques.

A substantial portion of the lands that are subject to aboriginal title claims are currently committed to a variety of licensed tenures held by forests products and mining companies. These *third party* resource interests are usually of a *usufructuary* rather than *proprietary* nature. Nevertheless, they are subject to possible attenuation in the land claims settlement process. That is to say, land claims settlements may require the *taking* of these resource interests from existing tenure holders, as Crown lands become settlement lands held in *fee simple* by a particular First Nation. Compensation may or may not be required as a consequence of these *takings.*

Whether or not current tenure holders will be able to re-create their attenuated resource interests through negotiation with First Nations who have substantiated their aboriginal title claims in the treaty negotiation process will, of course, affect the degree to which compensation is required for *takings* of these *third party* resource interests. Re-creation of these resource rights will depend upon the extent to which particular First Nations are interested in the further development of their settlement lands, and the extent to which they are interested in pursuing this development in partnership with existing tenure holders. This will, no doubt, vary from one First Nation to another.

Independent of the resource use decisions that particular First Nations will need to make, if they substantiate aboriginal title in a form that is equivalent to *proprietary ownership* of settlement lands, the Provincial Government will lose the benefit of the flow of stumpage charges, royalty payments and/or leasehold revenues from these lands. These resource revenues will, instead, flow to particular First Nations should they choose to continue the active exploitation of the natural resources contained within these lands. It follows that, whether or not compensation is payable to *third parties* for their attenuated resource rights, the average non-aboriginal taxpayer in the Province will be somewhat poorer as a result of the redistribution of *resource rents* to particular First Nations, especially if First Nations peoples continue to retain non-taxable status while resident on settlement lands. Either tax burdens will increase, or government service provision and support for the public infrastructure will be curtailed.

It is the purpose of this presentation to examine the consequences of both the *Delgamuukw* decision, and the *Nisga'a Final Agreement* if used as a template for other aboriginal title settlements, for the valuation of resource tenures within British Columbia. The presentation begins with a brief description of the current system of land tenure and resource use, especially as it pertains to forest and mineral tenures within the Province. It then proceeds to examine the nature of aboriginal title, and the tests under which aboriginal title can be established, in the light of the Supreme Court's *Delgamuukw* decision. A brief analysis of the *Nisga'a Final Agreement,* and a reconsideration of its value as a template for other aboriginal title settlements, follows.

The presentation then discusses the attenuation or replacement question for *third party* resource interests, and considers the issue of compensation for *takings* of these resource interests, if they occur. The implications of the numerous claims to aboriginal title for the valuation of resource tenures, both in the aggregate and in the specific, are then examined in the light of the *Delgamuukw* decision and the *Nisga'a Final Agreement* as potential template.

Finally, a brief overview of the financial implications of aboriginal title settlements, from the perspective of B.C.'s non-aboriginal population, is presented. This overview leads to the conclusion that the Federal Government, which has jurisdiction over Canada's relationships with its aboriginal peoples, may ultimately need to legislate an upper bound to the magnitude of these settlements, when taken in the aggregate, in a manner which will indirectly place a cap on the total land transfer to First Nations claimants within British Columbia. The Supreme Court's *Delgamuukw* decision, unlike the *Nisga'a Final Agreement* if used as a template, has created a substantial likelihood that a racially-based *rentier society* could be created within the Province. It is the Federal Government's responsibility to provide assurances to B.C.'s non-aboriginal population that the consequences of this outcome, if it materialises, are kept within manageable bounds.

2. *Current Systems of Land Tenure and Resource Use*

Systems of property rights in land and natural resources can be classified by their basic characteristics, which include comprehensiveness, exclusivity, durability, security, transferability and net benefits conferred. The strength of the bundle of property rights embedded in a particular land tenure arrangement can be measured by the extent to which each of these characteristics is present. In the case of forest tenures in B.C., the ranking of the *timber rights* associated with major forms of forest tenure appears to be, from strongest to weakest:

(a) private forest lands held in *fee simple* ownership,

(b) lease-hold interests (at present, almost no examples exist within the B.C. forests sector),

(c) timber licences outside tree farm licences,

(d) timber licences within tree farm licences (Schedule A lands),

(e) tree farm licences (Schedule B lands),

(f) timber sale licences within the Small Business Forest Enterprise Program (SBFEP), and

(g) forest licences.

With the exception of private forest lands held in *fee simple,* none of these forest tenures involves ownership of the land itself. Land ownership is vested in the Provincial Crown, although in many instances this ownership may be encumbered by claims of aboriginal title. Moreover, none of the tenures listed from (c) to (g) above involve property rights in land that are as strong and encompassing as a long-term lease would be. Indeed, with the exception of timber licences, which have evolved from the old temporary tenures that were established in B.C. prior to the beginning of 1908, these property rights fall short of *proprietary ownership* of the standing timber, let alone the land on which the timber is located. The *third party* property rights that exist in Crown timber are clearly *usufructuary* in nature. Moreover, they come with a variety of tenure obligations associated with harvesting regulations, silviculture applications and reforestation objectives.

The first six of these tenure forms are area-based, and the seventh is volume-based, implying as it does a certain allowable annual cut (AAC) quota within a particular timber supply area. Putting the possible, but unrepresented, lease-hold interest on one side, the strongest *usufructuary* right is that of the *profit à prendre* or share-cropping interest in land that applies in the case of timber licences. A timber licence provides an exclusive legal right to take a potential profit from the mature timber stands contained within the timber licence acreage, conditional upon the right of the Crown to set the terms and conditions under which the property right may be exercised. A timber licence is both transferable and durable, but provides no comprehensive right to the land itself, nor to any of the resources, other than timber, that the licensed acreage might shelter.

Timber rights, or resource interests in inventories of standing timber, possess market value for tenure holders. This market value may be called an *option value.* The sources of this option value are threefold. The first source relates to the freedom to choose when to harvest timber stands contained within a particular licensed acreage. This freedom is circumscribed by harvest regulations that are embodied within AAC restrictions, and by the necessity to have forest management and associated logging plans approved by the Ministry of Forests before cutting permits are issued. Nevertheless, within these regulatory limits, there remains some freedom to choose when harvesting will actually occur.

The second source of option value relates to the provision of secure supplies of wood fibre to the appurtenant processing mills in which an integrated forests products firm has usually invested significant capital resources. The security of these fibre supplies may enhance the ability of management to operate these conversion mills in an efficient and profitable manner. Most particularly, the security of fibre supplies may lead to optimal decisions with respect to the utilisation of mill capacity.

The third source of option value relates to the willingness (or lack of willingness) of the Crown to forego the capture of forest resource rents. It is this third source of option value which distinguishes an option to cut from an option to share in the potential economic rents that may arise from product price increases, and which can most appropriately be referred to as a *profit à prendre.* For timber licences, this last component can, in principle, be measured by the difference between stumpage prices and royalty rates for equivalent timber, while this narrowing difference continues to exist. More generally, however, the third component would exist for any licensed tenure where Crown stumpage charges failed to capture full economic rent.

The *option value* of timber rights is a private market value which is distinct from, and additive to, the stumpage value of the associated timber inventories to the Crown. This market value can best be approximated by estimating the net present value of these inventories, after appropriate allowance for the Crown charges (stumpage or royalties) that are applied as the timber is harvested. This net present value depends upon the future harvest plan for the net operable timber inventory, incorporating an appropriate allowance for forest management restrictions and for wastage, the forecast future prices of the timber when cut, the estimated future harvesting costs including log hauling and other transportation costs, and the costs of any reforestation and silviculture obligations that need to be fulfilled before the specific licence reverts to the Crown. Each of these elements in the future pattern of receipts and outlays should be brought into present value terms by using an appropriate risk-adjusted discount rate or *hurdle rate of return.*

Just as forest tenures provide *usufructuary* property rights to tenure holders, so too do mineral leases and exploration licences. Although an exploration licence is a fairly limited form of property right, under certain conditions it may be convertible into a mineral lease. A mineral lease generally

provides property rights to resource pools or to ore bodies that are stronger than those contained in most Crown forest tenures. In general, a lease-hold interest in land conveys a more comprehensive, exclusive and (possibly) durable property right than that of a *profit à prendre*, and certainly than that of a licence. However, a lease-hold interest still falls short of a free-hold or *fee simple* interest in land from the perspective of characteristics such as comprehensiveness, durability and (possibly) transferability.

3. *Aboriginal Title and the Delgamuukw Decision*

As previously indicated, there can be no question that the judgement of the Supreme Court of Canada in *Delgamuukw v. British Columbia* has pushed the definition of aboriginal title further towards a *proprietary ownership* concept and away from the alternative *usufructuary rights* concept. The differences between these two concepts are illustrated in the following chart, which relates to the classification of resource goods, and to the inter-temporal evolution of property rights with respect to these resource goods.

Classification of Resource Goods

	non-excludable	***excludable***	
non-rival	public resource goods	club/toll resource goods	time ↓
rival	congested common pool resource goods	private resource goods	
nature of property right	*usufructuary*	*proprietary*	

In this context, resource goods are classified into those for which individuals hold *proprietary ownership rights* and, as a result, are able to *exclude* others from consuming them, as distinguished from those where *non-excludability* is the rule and property rights take, at most, the *usufructuary* rather than the *proprietary* (or free-hold) form. Resource goods are also classified by the degree to which their consumption is *rival* or *non-rival.* As time has passed, resource goods which were previously non-rival in the relatively uncongested world of the historical past have become rival in consumption as congestion has increased the pressure on land and resources. Over time, increasing congestion turns *public goods* into *congested common pool resources* and *club goods* into *private goods.* Thus, *public goods* are both non-excludable and non-rival, *congested common pool resources* are non-excludable and rival, *club goods* (which are sometimes also referred to as *toll* goods) are excludable and non-rival, and *private goods* are both excludable and rival in consumption.

Delgamuukw v. British Columbia pushes towards the view that aboriginal title historically involved the right to consume *club goods,* for which membership in the *aboriginal club* was a necessary prerequisite for access. As time has passed, and congestion on land and resources has become more rival and intense, these *club goods* have, on this view, become akin to *private goods,* to which particular First Nations have *exclusive proprietary ownership rights.* The alternative view is that aboriginal title historically involved the right to the non-rivalrous consumption of *public goods,* which were abundantly available because harvest volumes were constrained by the low productivity of traditional technologies. As time has passed, and high productivity harvesting technologies have been developed, increasing pressure on land and resources has, on this alternative view, turned these *public goods* into *congested common pool resources* to which *usufructuary access rights* need to be rationed by the Provincial Government through various allocative processes.

Quite clearly, these two different viewpoints lead to quite different concepts of aboriginal title in today's world, with very different implications with respect to the appropriate *distribution* of the *resource rents* that are available within the Province. These *resource rents* have both a quantitative dimension and a unit price, which represents the unit value of the right of access to increasingly congested Provincial resources. *Capital gains* become available as this unit resource rental value (or user cost) increases over time. Essentially, the aboriginal title settlement process will provide an explicit answer to the question, *"who is entitled to share in this capital gain?"*

First Nations people will argue that land and resources were originally taken from them without due process or compensation and, therefore, that they are entitled to the *capital gain* on lands and resources which have implicitly been held for them in trust by the Provincial Crown. Non-aboriginal British Columbians will alternatively argue that the *capital gain* has occurred only because of the investment of physical and human capital, and the application of modern technologies, to land and resources that would be much less productive without these complementary inputs. Are the *capital gains* associated with rising unit resource rental values simply due to resource scarcity in an increasingly congested world, or are they a product of human and technological ingenuity applied to resource-using processes?

The theory of inter-temporal choice does not provide a one-sided answer to this question. Indeed, it supports the notion that there is an element of truth in both sides of the argument. In consequence, the appropriate sharing of the *capital gain* among the three percent of the Provincial population who are members of First Nations communities and the ninety-seven percent who are not is ultimately a question of both politics and distributional justice, rather than one of economics. Nevertheless, it is useful to conceptualise the aboriginal title settlement question as one of sharing the *capital gain* made available by the inter-temporal appreciation of Provincial natural resource values and associated *economic rents.*

It is, of course, quite possible that these potential rents will be dissipated in legal wrangles, and by the investment-reducing uncertainties that surround land ownership in British Columbia. These uncertainties will continue until the numerous aboriginal title claims are resolved, either by treaty negotiations or by rent-dissipating litigations, and what ultimately remains of Crown land is unburdened of aboriginal title claims. Nevertheless, if we follow the Supreme Court's *proprietary ownership* view of aboriginal title, as opposed to the alternative *usufructuary rights* view, we are likely to establish a racially-determined *rentier society* in British Columbia, in which *resource rents* no longer belong to B.C. residents at large, through their Provincial Government, but instead belong to particular First Nations people.

There can be little doubt that the majority viewpoint enunciated by the Supreme Court of Canada is one that supports the *proprietary ownership* concept of aboriginal title. In *Delgamuukw v. British Columbia,* Chief Justice Antonio Lamer has defined aboriginal title in the following manner:

"Aboriginal title encompasses the right to exclusive use and occupation of the land held pursuant to that title for a variety of purposes, which need not be aspects of those aboriginal practices, customs and traditions which are integral to distinctive aboriginal cultures. The protected uses must not be irreconcilable with the nature of the group's attachment to that land. ... Aboriginal title is ***sui generis,*** *and so distinguished from other proprietary interests, and characterized by several dimensions. It is inalienable and cannot be transferred, sold or surrendered to anyone other than the Crown. ... Aboriginal title is held communally. ... Aboriginal title is a burden on the Crown's underlying title. ... Aboriginal title is a right to the land itself."*

With respect to the tests that are necessary to establish aboriginal title, the Chief Justice has written as follows:

"In order to establish a claim to aboriginal title, the aboriginal group asserting the claim must establish that it occupied the lands in question at the time at which the Crown asserted sovereignty over the land subject to the title. ... Under common law, the act of occupation or possession is sufficient to ground aboriginal title. ... If present occupation is relied on as proof of occupation pre-sovereignty, there must be a continuity between present and pre-sovereignty occupation. ... An unbroken chain of continuity need not be established between present and prior occupation. ... At sovereignty, occupation must have been exclusive."

Finally, with respect to previous litigation at the Provincial level and the nature of evidence, to the issue of the fiduciary relationship between the Crown and aboriginal peoples with respect to infringements of aboriginal title and the duty to consult, and to the matter of the authority to extinguish aboriginal rights, the Chief Justice has also written:

"The oral histories were used in an attempt to establish occupation and use of the disputed territory. ...The trial judge refused to admit or gave no

independent weight to these oral histories. ... Had the oral histories been correctly assessed, the conclusions on these issues of fact might have been very different. ... There is always a duty of consultation and, in most cases, the duty will be significantly deeper than mere consultation. ... Fair compensation will ordinarily be required when aboriginal title is infringed. ... Section 91(24) of the ***Constitution Act, 1867*** *(the federal power to legislate in respect of Indians) carries with it the jurisdiction to legislate in relation to aboriginal title, and by implication, the jurisdiction to extinguish it. ... A provincial law of general application cannot extinguish aboriginal rights."*

Together, these three sets of quotations from *Delgamuukw v. British Columbia* clearly change the nature of the playing field on which aboriginal land claim settlements will occur, at least in British Columbia. It is almost as if the Chief Justice believes that British Columbia consists of vast empty spaces that are unoccupied except for First Nations peoples and are uncommitted to the legion of tenure arrangements that provide *usufructuary access rights* to Crown lands and the resources they shelter. These *third party* resource interests are brushed aside by the Chief Justice in the grossly understated trio of sentences:

"This is an issue that may involve an assessment of the various interests at stake in the resources in question. No doubt, there will be difficulties in determining the precise value of the aboriginal interest in the land and any grants, leases or licences given for its exploitation. These difficult economic considerations obviously cannot be solved here."

A large, realistic infusion of economic wisdom, particularly as it pertains to Western Canada, seems urgently to be required in the most senior of Canada's judicial institutions. The economic geography of British Columbia bears little or no resemblance to that of Canada's northern territories, or that of the James Bay area of the Province of Quebec. Productive, but uncommitted, lands do not exist with the abundance that would be necessary to support large-scale reassignments of ownership and/or tenure.

4. *The Nisga'a Final Agreement as Template*

The *Nisga'a Final Agreement* is clearly a path-breaking achievement for each of the three negotiating teams. The fact that an Agreement has finally been achieved after many years of sustained activity by the Nisga'a Nation is very much to the credit of the Nisga'a people. They have demonstrated great patience and faith that a settlement would ultimately be achieved.

The *Nisga'a Final Agreement,* once ratified, will provide significant benefits for the Nisga'a people. These benefits have been reviewed in my *Laurier Institution* book chapter. At the time of writing that chapter, the Supreme Court's *Delgamuukw* judgement had not yet come down, and I took the position that the Nisga'a Agreement could not easily stand as a precedent or template for future B.C. settlements, because it involved an overall level of transfer costs,

and an associated redistribution of wealth and resource ownership, that would not be sustainable across all eligible First Nations claimants.

The *Delgamuukw* decision has changed my view on this. Indeed, the *Delgamuukw* decision has so escalated the expectations and bargaining strength of First Nations claimants that I would now argue that non-aboriginal British Columbians will be fortunate if other aboriginal title settlements can occur on a basis that is similar to the Nisga'a Agreement. Moreover, I believe that the Agreement will be ratified, and that it will be used, at least in a general way, as a template for future aboriginal title settlements in B.C.

In moving towards these future settlements, fundamental trade-offs between the financial components of individual settlements and the land transfer component will need to be made. Moreover, within the land transfer component, trade-offs will clearly also be necessary to balance the quantity of land transferred to *proprietary ownership* by particular First Nations with other land areas on which specific *usufructuary rights,* short of ownership in *fee simple,* are granted to First Nations people.

What we are here involved with, after *Delgamuukw,* is a massive exercise in redistributive social engineering. Most non-aboriginal British Columbians understand that redistributing resource wealth to First Nations is not only just, but also essential to the redress of past wrongs, given the unfortunate history of discrimination against First Nations peoples in B.C. However, most people also believe that there are limits to the amount of resources that are available for redistribution, even in cases where social conscience is a major motivating factor. It is here that the Federal Government has a major role to play in the re-establishment of reasonable expectations.

One of the more attractive features of the *Nisga'a Final Agreement* is the fact that, after a period of eight years after the *Agreement* comes into effect, members of the Nisga'a Nation will become liable for transactions or sales taxes, and, after a period of twelve years, will be liable for all other forms of taxation such as personal income taxes. However, some form of *equalisation payments* will be required, at least on a transitional basis, to supplement the own-source revenues that the Nisga'a Nation receives in the form of *resource rents* and local taxes, such as property taxes. These *equalisation payments,* which will support the on-going provision of social services to persons resident on Nisga'a lands, are to be negotiated at five-year intervals, and are quite separate and distinct from the $190 million (in constant 1995 dollars) transfer of *Nisga'a capital,* which is intended to complement the land transfer, and the other capital transfers to the Nisga'a Nation, which are associated with the Nass River fisheries. All of these financial arrangements are designed to ensure the viability of Nisga'a self-government, while regularizing (after a transitional period) the taxation status of individual members of the Nisga'a Nation.

5. *Third Party Resource Interests: Attenuation or Replacement?*

There can be no question that uncertainties about land ownership and the durability of tenure arrangements are one of the factors that are currently undermining the investment climate in B.C.'s resource industries. Resolving aboriginal title claims to specific tracts of land, and to the resources they shelter, is the only way to clarify the legal status of *third party rights* to use Crown lands and resources. In many instances, these rights may well be attenuated, although perhaps (as in the *Nisga'a Final Agreement,* for example, with respect to access to forest resources) after some fairly short phase-out period. During the phase-out period, if any, there may be opportunities to negotiate the replacement of these *third party* Crown resource interests with the new First Nations owners.

Third party usufructuary rights to Crown lands and resources involve resource interests that include:

(a) the right to harvest timber,

(b) the right to extract metallic ores and other mineral resources,

(c) the right to store and/or divert water for either consumptive or in-stream purposes,

(d) the right to graze livestock,

(e) the right to harvest wildlife, migratory birds, and fish species, and

(f) the right to control access to recreational resources.

All of these resource interests possess some economic value, although the licences which convey these rights are ordinarily time-limited. Some, but not all, of these licences are transferable, but often only with the permission of the relevant Minister. In some instances, resource rights are conveyed only with associated obligations, which normally reflect conservation requirements and/or environmental concerns.

In the forests sector, at least three major *third party* concerns need to be resolved. The first of these is how the treaty settlement process will affect the industry's ability to operate efficiently, and without major delays, in harvesting timber on Crown lands. The second is how treaty settlements will affect forest tenures and allowable annual cuts in various timber supply areas. The third involves what access the industry will have to timber resources on lands that are to be transferred to aboriginal communities, and in particular what stumpage charges and other costs will have to be paid for this access. At present, answers to all three of these concerns remain unclear, and this is adding to the uncertainties that surround resource-related investments in B.C. Much will depend upon individual circumstances, and the interests particular First Nations have in the formation of resource-development partnerships with existing firms within the industry.

Where partnerships appear to be viable, attenuated resource interests may be re-created by particular First Nations on settlement lands transferred to them as *proprietary owners.* In this case, *resource rents* previously paid to the Provincial Crown will instead be paid to the particular First Nations community. This will, inevitably, increase the tax burden on other Provincial residents, although *third party* compensation for the loss of a Crown resource interest would not seem to apply. However, in other situations, it may not prove to be possible to re-create attenuated resource interests. In these situations, the Crown (and Provincial taxpayers) will be burdened not only with the loss of potential *resource rents,* but also with the costs of any compensation sums that may need to be paid for the attenuation of *third party* resource interests.

In cases in which there is no automatic right to the renewal of a licensed resource interest, much will depend upon the date at which the existing access licence expires in relationship to the date at which settlement lands containing the resources in question are transferred to First Nations communities. If the access licence expires before the transfer date, no compensation may need to be paid. This creates some need to negotiate transitional arrangements whereby *third party* access rights are only gradually phased-out by the Crown, in order to minimise potential compensation costs. In cases in which there is a contractual right to the renewal of an existing licence, however, the minimisation of compensation costs may not be achievable by this route. This implies that the durability of *third party* resource interests is likely to be an important issue in the determination of overall compensation costs.

6. *The Compensation Question*

The *Report of the Commission of Inquiry into Compensation for the Taking of Resource Interests* (the Schwindt Commission of 1992) created a lively debate within B.C. on the question whether or not compensation should be paid by the Crown when *third party* resource rights are attenuated, and what form any such compensation should take. The issue is clearly different from the question of compensation for the expropriation of lands held in *fee simple,* since only *usufructuary* rather than *proprietary* resource rights are involved.

In the case of mineral rights, such as mineral leases and exploration licences, only very recently has the Provincial Government moved to provide legislation that would protect these resource rights, which are generally quite site specific. However, the earlier settlement with Royal Oak Mines Ltd., in compensation for its loss of a significant mining opportunity when the *Tatshenshini-Alsek Wilderness Park* was created, signalled that the B.C. Government would be moving towards legislation which would embody a presumption of compensation in the case of mineral resource interest attenuations.

In the case of *timber rights,* the *Forest Act* allows for partial compensation for the taking of resource interests in Provincial timber

inventories. More explicitly, section 60 of the *Forest Act* indicates that the Crown may restrict operable timber volumes by deleting areas from within existing licences or by reducing a licence's allowable annual cut (AAC), either

> (i) for the purposes of access to Crown timber, highway, pipeline or power transmission line rights of way or of water storage; or
>
> (ii) for a purpose other than referred to in subparagraph (i) and other than timber production.

In either of these instances, within any given deletion period, only deletions that affect more than five percent of the licence area or five percent of the licence's AAC are compensable, and then only for the portion of the deletion that exceeds the five percent threshold. In addition, improvements made to Crown lands that are authorised, but not paid for, by the Crown are also compensable. Here the main consideration is likely to be unamortised road development costs that were incurred before the valuation date. Notice, however, that reductions in AAC that occur through the regular timber supply review process are *not* compensable under the *Forest Act.* Where agreement with respect to the amount of compensation cannot be otherwise attained, the processes outlined within the *Commercial Arbitration Act* are to be applied.

There are those who would argue that potential *takings* of forest resource interests involve no more than normal (and presumably insurable) business risks. They, therefore, take the view that these *takings* should *not* be compensable in the normal course of events. Companies holding a large number of Crown tenures may be able to self-insure against small, unconcentrated, attenuations of their resource interests. This is unlikely to be the case for smaller tenure holders. In addition to this, *takings* of *timber rights* tend to be concentrated in particular geographic areas, as illustrated by recent *takings* for park creation. This *lumpiness* tends to make for uninsurability, because the *averaging-out* of impacts is unlikely to occur.

There are others who would argue that *takings* do not occur unless the cancellation of previously issued cutting permits is involved. Although this approach might have some merit in the case of volume-based tenures, such as forest licences, it fails to recognise the *usufructuary* property rights that exist in specific tracts of land in the case of area-based tenures, such as tree farm licences. In the case of timber licences, it also fails to recognise the *proprietary* ownership of the mature timber inventory, conditional upon the Crown's right to receive royalties and/or stumpage payments when the timber is harvested from *its* land.

The conclusion that emerges from this brief analysis is that, generally speaking, *takings* of *timber rights* are partially compensable under the *Forest Act.* Other than the element of compensation for improvements made to Crown land, compensation should in most instances be limited to the *option value* of the attenuated *timber rights,* as measured by the net present value, to private sector participants, of the affected timber inventories. Provided that Crown

charges do adequately capture available forest resource rents, this *option value* will not contain an element of compensation for uncollected rents.

It is, however, important to note that section 60 of the *Forest Act* does not allow for the possibility that *takings* could occur to create timber production opportunities for other persons, for example, First Nations communities. Presumably, in the interests of a level playing field, the Crown is not, under normal circumstances, supposed to take a timber interest from one tenure holder in order to create a similar timber interest for another industry participant. The *Forest Act* is, therefore, silent on the issue of compensation for *takings* of *timber rights* that may be required to unburden lands that are to be transferred to First Nations in the aboriginal title settlement process. Indeed, the *Forest Act* would apparently need to be amended if section 60 is to become applicable to this situation.

7. *The Valuation of Resource Interests*

There are three generally accepted appraisal methods that could be used for the valuation of timber inventories from the perspective of tenure holders or potential purchasers of harvesting rights to Crown timber resources:

(a) the investment cost method,

(b) the sales comparison method, and

(c) the present value of net income method..

For most purposes, including situations in which compensation is being contemplated for the *taking* of a resource interest, the present value of net income method is the most appropriate one to use. This method uses a discounted cash flow (DCF) approach to estimate the present value of the net income stream that is attributable to the timber inventories in question.

Of the other two approaches to the estimation of market value, the investment cost approach is better used to determine the replacement costs of fixed capital assets than to determine the market value of timber harvesting rights. The sales comparison method can, in principle, provide a market value estimate, but sales transactions that are truly comparable are difficult to identify even if they exist. The problem is that most trades of access rights to timber appear to be components of package deals from which it is difficult, if not impossible, to unscramble uncontaminated market prices for the access rights themselves. Thus, the use of this method is generally limited to providing an independent check on the DCF approach to market value.

The DCF method can be used to calculate the present value, as at an effective valuation date, of the net income stream attributable to an assumed harvest schedule for the timber inventory in question. (The harvest schedule may, of course, be substantially but not entirely governed by an existing AAC determination.) This present value is an estimate of the market value of the

timber inventory on the valuation date. Reasonable expectations based upon information that was actually available on the valuation date (and not based upon hindsight or upon an information set pertaining to some other date) should be used in the estimation of market value. The calculation should ordinarily be carried out in real terms, using an appropriate real (or inflation-adjusted) after-tax discount rate to convert the stream of annual cash flow returns into a net present value.

The basic data requirements of the DCF approach to market value are as follows:

(a) timber quantities, or an estimate of the net operable mature timber inventory (measured in cubic metres),

(b) timber prices,

(c) harvesting schedule,

(d) harvesting costs,

(e) Crown charges,

(f) discount rate, and

(g) taxation parameters

Provided that these seven basic data requirements are fulfilled, the DCF method can provide an estimate of the market value of the *timber rights* associated with licensed access to particular standing timber inventories, or the *option value* of the particular Crown tenure. It is important that the data utilised contain no obvious biases, especially with respect to cyclical peaks and troughs in timber (or log market) prices and, possibly, in harvesting costs. Cyclically-averaged data should ordinarily be used. Numerous other technical issues associated with the *valuation of timber rights,* including taxation issues, are discussed in my consulting report on *Forest Resource Rents and the B.C. Timber Pricing System.*

The issue of *disturbance damages* should also be considered. *Disturbance damages* refer to losses in the value of a property right that result from impending or threatened regulatory action. These damages may pre-date the statutory action that usually consummates the *taking* of a *usufructuary* resource interest. In the case of land-use planning processes that eventually lead, for example, to the creation of new Provincial parks, specific timber rights may be progressively depreciated as the risk that particular timber inventories may not be harvestable begins to be perceived. Indeed, harvestability risks that become certainties will reduce the *option value* associated with the timber rights to these particular inventories essentially to zero.

Deletions of particular land areas from active forestry to meet environmental objectives may lead to more effective zoning of other forest lands in the same general vicinity for active timber production. This potential gain in tenure security amounts to a reduction in uncertainty with respect to the harvestability of other timber resources. When a process of reconciling

competing land-use objectives is completed, any gain in tenure security that licence holders may acquire with respect to their remaining timber rights provides, to industry as a whole, a possible offset to site-specific and company-specific *disturbance damages.*

The beauty of the discounted cash flow (DCF) or net present value approach to the estimation of compensable market value in these circumstances is that it essentially treats the particular timber inventories *as if* they were located elsewhere, on land not subject to park development (or transfer to First Nation's ownership), and thus continue to be harvestable. It does not, therefore, discount for the specific risks that have pertained, perhaps in an escalating way, to the harvesting possibilities for the particular timber inventories in question. *Disturbance damages* are, therefore, not additive to DCF-determined market values. Indeed, they are largely captured within these values. The use of earlier valuation dates relating to regulatory interference with harvesting rights, which could turn out to be temporary, rather than later valuation dates relating to statutory interference with these rights, which is ordinarily permanent, is largely unjustified as an approach to the recapture of *disturbance damages.* It may, of course, be a way of adding larger statutory interest accruals to compensation settlements.

Several years ago, through an arbitration process pursuant to section 60 of the *Forest Act,* compensation was arranged for forest tenure *takings* that occurred in association with the creation of the *South Moresby Gwaii Haanas National Park Reserve.* Compensation is required under section 60 of the *Forest Act* by the terms of the *Carmanah Pacific Park Act,* but has not yet been arranged. The *Park Amendment Act, 1995,* is silent on the question of compensation for *takings* necessitated by the implementation of the *Vancouver Island Land Use Plan,* and on the issue whether or not section 60 of the *Forest Act* pertains to these attenuations. Although some negotiations with respect to these park-related tenure attenuations have occurred, as yet there seems to be no clearly enunciated policy which would identify either the process, or the formula, that might be applied in these potentially compensable situations, despite section 60 of the *Forest Act,* the *Schwindt Report*, and previous precedents.

One of the reasons why the Provincial Government may be taking a cautious approach to the question of compensation for park-related attenuations of forest tenures is that it may be concerned about the precedential implications of potential compensation awards for *third party* claims that may arise from the aboriginal title settlement process. The *third party* compensation bill that could result from the aboriginal title settlement process is potentially very large, and could involve significant claims for *disturbance damages,* depending upon the progress of First Nations treaty negotiations.

What, then, are the implications of the *Delgamuukw* decision for the valuation of resource tenures in British Columbia? First and foremost, the security of most *third party* resource tenures has been reduced by the *Delgamuukw* decision. In particular, the *Delgamuukw* decision has increased

the likelihood that court injunctions will be used by First Nations to block resource developments on lands which are subject to aboriginal title claims. It has also made it less likely that *third party* resource tenures will be renewed at the end of their term, or at the appropriate renewal or roll-over date. These effects serve to reduce the value of these tenures to *third parties* and, therefore, to undermine the incentive to invest in resource-related capital projects in the Province.

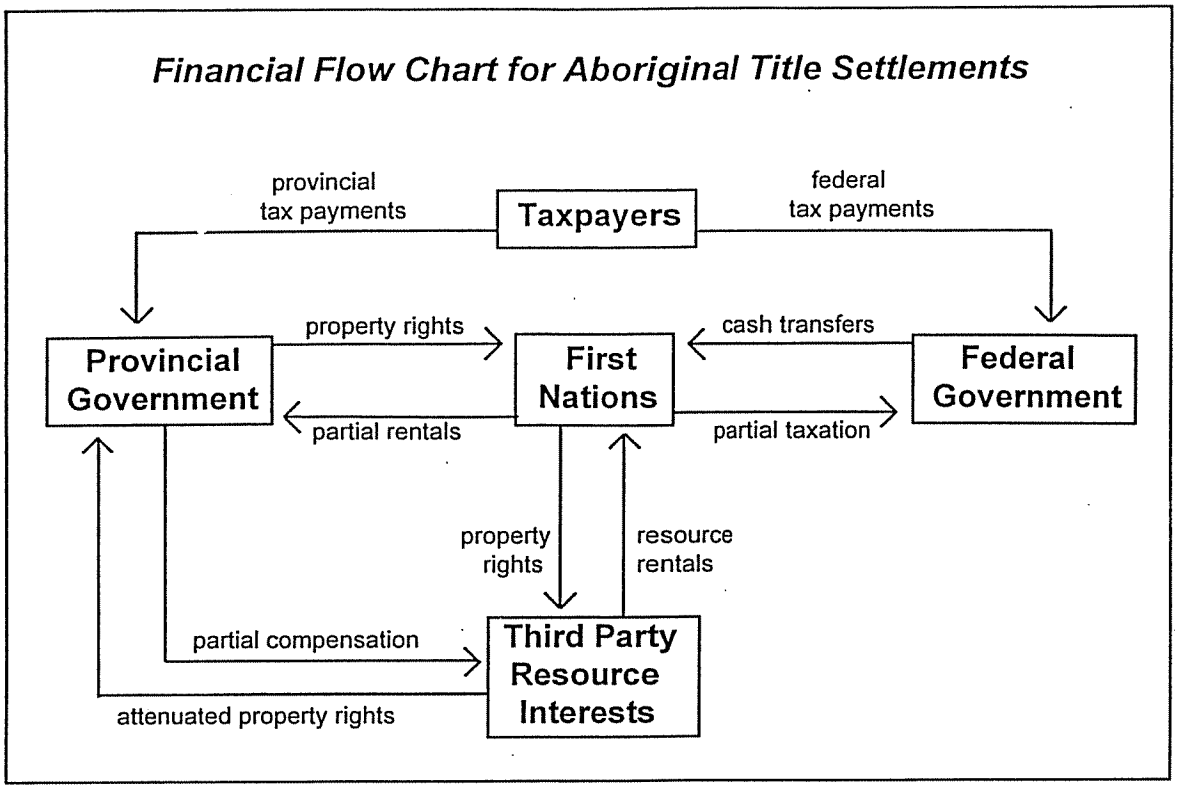
Thus, the *Province-wide* impact of the *Delgamuukw* decision is to reduce the value of *usufructuary* property rights to Crown resources, largely because of the increased uncertainty whether these resources actually belong to the Crown. This reduction needs to be measured against a general tendency for the social value of rights to use the Province's natural resources to increase over time. In situations where the *Delgamuukw* decision leads particular First Nations to the greater exercise of confrontational techniques, including the use of court injunctions, there will also be negative *site-specific* impacts on the *option value* of *third party* resource interests. However, where access to Crown resources is not burdened by aboriginal title claims, the *site-specific* impact is likely to be positive.

As the treaty negotiation process begins to clarify what lands are to be transferred to First Nations communities, and what lands are not, the *option value* of *site-specific* resource access on Crown lands that are unburdened of aboriginal title claims is likely to increase. This is, of course, one of the reasons why the business community is in favour of settling land claims rather more quickly than is likely to be the case. The *Delgamuukw* decision creates greater pressure to settle questions of aboriginal title within the Province. However, its expectational impacts also greatly increase the political-economic difficulties in reaching treaty settlements that all parties to the negotiation process will consider to be reasonable.

As previously mentioned, it is the responsibility of the Federal Government to restore reasonable expectations in the light of the Supreme Court's *Delgamuukw* decision. At the moment, the Federal Government does not seem to believe that it would be *politically correct* to take any actions that would restore reasonable expectations, although it would be good party politics. The Provincial Government has no jurisdiction to take legislative action related to the First Nations of British Columbia.

8. *Financial Implications of Title Settlements*

The basic financial framework for treaty settlements in B.C. is best illustrated in graphic terms. The following flow chart identifies five major parties: the Federal Government, the Provincial Government, First Nations, taxpayers and *third party* resource interests.



Taxpayers provide the funds for both the Provincial and Federal Governments. Since Canadian taxpayers will bear most of the costs of First Nations treaty settlements, they will have to pay additional taxes (or equivalently experience a reduction in public service provision). The Federal Government will need more tax revenues to finance a stream of cash transfers to First Nations groups. However, if First Nations groups gradually lose their non-taxable status as part of the settlement process, or lose access to special government services, they will, in effect, transfer some (but not all) of that cash back. (For simplicity, the flow chart does not show the parallel transfer of cash to and from the Provincial Government, or the Province's cash contribution to the settlement.)

The Provincial Government will arrange to transfer property rights in land and resources to First Nations. Although these property rights transfers are transfers-in-kind, they will diminish the Provincially-owned stock of resources, and reduce the flow of resource rents to the Provincial Government. Some partial resource rental returns may accrue to the Provincial Government with respect to *usufructuary* property rights transfers, but these returns will not materialise for all *proprietary* or *fee simple* land transfers. In consequence, the Provincial Government will need to replace its loss of natural resource revenues by imposing additional taxes on Provincial residents. These will probably not be taxes on resources, because the land and resource transfer itself will undoubtedly lower the Province's ability to increase such taxation.

The process will also involve the attenuation of *third party* resource interests held by the private sector. The Provincial Government will need to pay partial compensation for these *takings*. The larger is the compensation bill, the

larger will be the burden of the aboriginal title settlement process on Provincial taxpayers. Indeed, the Provincial Government faces an acute trade-off between the degree to which it burdens *third party* resource interests with the costs of aboriginal title settlements by failing to pay adequate compensation for the attenuation of resource interests, and the degree to which it burdens Provincial taxpayers with these costs.

First Nations groups may re-create *third party* access rights to land and resources, in a manner which would reduce the Province's compensation bill. Resource rents would then flow from the private sector to First Nations communities to pay for this renewed access. If these new arrangements between First Nations communities and *third party* resource interests are of mutual benefit and are entered into freely, then the value of the renewed access to resources will be equal to the flow of resource rents.

Given this equality, and the assumption that both the Federal and Provincial Governments arrange their finances on a break even basis, the gain to First Nations will be equal to the additional Federal revenues raised from non-aboriginal taxpayers plus the net value of the property rights to land and resources transferred to them. The loss to *third parties* will be represented by the degree to which their attenuated (and not re-created) resource interests remain uncompensated. The loss to non-aboriginal taxpayers will be the additional tax payments made to both orders of Government.

The flow chart essentially portrays the financial framework for aboriginal title settlements as a *zero-sum* game. However, there are normally *dead-weight losses* associated with the additional tax burdens and transactions costs arising from all major redistributive exercises. Offsetting these losses are the *potential gains* in Provincial economic activity which may result from the reduction in tenure uncertainty as aboriginal title settlements are actually completed. Whether or not these *potential gains* will offset the *dead-weight losses* remains to be seen.

Indeed, those who have asserted that *prospering together* will be the likely outcome of the land-claims settlement process in B.C., should reflect upon the fact that Federal cash transfers are not *manna from heaven.* There is ultimately only one taxpayer and *no free lunch.* Although the spending of cash settlement monies by First Nations people may create more local employment opportunities, these additional jobs will be offset (and probably more than offset) by the loss of jobs associated with smaller Government expenditures in other directions, or by higher taxation levels, or both.

It is optimistic to believe that the savings in social spending and the benefits of new economic development will more than offset the costs of settlement. Put differently, the land claims settlement process, which is fundamentally redistributive in nature and associated with the remedying of past injustices, should not be oversold as a *win-win* process. Nevertheless, the more that the treaty settlement process leads to the creation of productive new opportunities for economic development that can best be pursued by

partnership arrangements between First Nations communities and non-aboriginal business ventures whose operations require access to certain natural resources, the more smoothly will the transition occur. To this end, First Nations could use some of the cash and resource transfers received in treaty settlements to create resource development corporations that could readily enter into partnership arrangements with non-aboriginal businesses. The voting shares in these development corporations could be held by members of the particular First Nations community.

If this were to be the chosen structure for a First Nations development corporation, it would probably be treated as a registered private company and, therefore, would be subject to corporate income tax. However, a corporation that is entirely owned by a First Nations government rather than by individual shareholders would probably not be similarly taxable, since according to the Constitution of Canada no one government can impose direct taxation on another government. Thus, by appropriate structural design, development corporations (like Provincial Crown corporations) could escape direct taxation by other levels of government. Consistent with this principle, the *Nisga'a Final Agreement* specifies that Nisga'a Lands will be exempt from provincial property and resource taxation in perpetuity.

9. Concluding Remarks

Financing First Nations treaty settlements in B.C. will undoubtedly be expensive. Yet we must proceed with them, not only because First Nations aboriginal rights have not been extinguished within B.C., but also because we must treat First Nations peoples equitably. Resolving land claims settlements is the only way to clarify the legal status of *third party* rights to use Crown land and resources. Clear definitions of aboriginal property rights, and the sorting of these resource rights in specific situations into those which are *proprietary* and those which are merely *usufructuary* in nature, are both required. The greater is the clarity of these determinations, the less is the potential for future conflicts over land use, as access to the Province's resources becomes increasingly congested.

Transferring *fee simple* ownership of existing reserve lands to First Nations peoples, and adding major additional parcels of Crown lands adjacent to these reserves to the *fee simple* transfer, would certainly clarify the question of who has legal title to these lands. Granting further rights to use and profit from other Crown lands that are consistent with how First Nations have traditionally used these lands would also help to clarify what rights, short of *fee simple* ownership, apply in these contested areas. Trade-offs will clearly be necessary to balance the amount of land transferred to *proprietary* ownership, the amount of land on which *usufructuary* rights to Crown resources are conveyed, and the exact definition of these land use rights. The onus will be on the Provincial Government to make sure that these trade-offs make sense from the perspective of *all* British Columbians.

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