Limits on the fee simple interest

Contrasting expropriation and police powers

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This article reviews a recent decision of the British Columbia Supreme Court that provides an example of the power local government wields to appropriate the property rights of landowners through 'downzoning' without compensation. From a valuation perspective, how does an appraiser accommodate this ever-present risk?

The case in question is *V.I.T. Estates Ltd. v. New Westminster (City)*, 2021 BCSC 573 [*VIT*]. Before turning to the case, some context is perhaps useful. Appraisers know that the fee simple interest in real property is the most complete form of ownership and that it is subject only to four powers of government:[1]

- taxation;
- expropriation;
- police power; and
- escheat.

The focus here is on expropriation contrasted with an aspect of police power, namely zoning.

One of the long traditions of the common law is the protection of private property rights. A consequence of this tradition is the common law presumption that when a government expropriates real property, compensation must be paid. Only if there is a specific provision in legislation to the contrary will the presumption be rebutted.[2] Compensation is provided either in accordance with expropriation legislation or as an incident of *de facto* expropriation. [*De facto* expropriation requires two elements: 1) an acquisition of a beneficial interest in the property or flowing from it, and 2) removal of all reasonable uses of the property.[3]]

Local governments are enabled through local government legislation to expropriate property. By way of example, in British Columbia the *Community Charter*, SBC 2003, c. 26, sections 31 to 34 and the *Local Government Act*, RSBC 2015, c. 1, sections 289 to 292 allow local governments to expropriate real property interests with provision for compensation.

Contrast expropriation with the exercise of police powers in the form of zoning. Police power is defined as follows:[4]

> Police power is the right of government through which property is regulated to protect public safety, health, morals and general welfare. Examples of police power including zoning ordinances, use restrictions, building codes, air and land traffic regulations, public health codes, and environmental regulations.

There could be an argument, in the case of zoning for example, that the exercise of police power is *de facto* expropriation requiring the government to compensate affected landowners. Perhaps foreseeing this possibility, governments provide protective legislation. In British Columbia, the *Local Government Act*, RSBC 2015, c. 1 section 458 provides:

> **458** (1) Compensation is not payable to any person for any reduction in the value of that person's interest in land, or for any loss or damages that result from any of the following:
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> (a) the adoption of an official community plan;
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> (b) the adoption of a bylaw under
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> (i) Division 5 *[Zoning Bylaws]*,
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> (ii) Division 12 *[Phased Development Agreements]*, or
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> (iii) Division 13 *[Other Land Use Regulation Powers]*;
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> (c) the issue of a land use permit;
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> (d) the termination of a land use contract under section 547 *[termination of all remaining land use contracts in 2024]*;
>
> (e) the adoption of a bylaw under section 548 *[process for early termination of land use contract]*.
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> (2) Subsection (1) does not apply in relation to a bylaw referred to in paragraph (b) of that subsection that restricts the use of land to a public use.

But for the limited exception in subsection 458(2), the protection the law affords to expropriated parties is not available – at least in British Columbia – to parties who have had their property rights stripped from them by other means (e.g., zoning).

The upshot is that a local government has the means to diminish the use of your property and its value without compensation. If done in compliance with enabling legislation and stipulated procedures are followed, a property owner has no recourse except at the ballot box.

This brings us to *VIT*. V.I.T. Estates Ltd. owned 237 strata units in six residential buildings ('Six Buildings') located in the City of New Westminster, British Columbia that were rented by the owner pursuant to the *Residential Tenancy Act*. In 2010, the City adopted an Affordable Housing Strategy having as one of its goals the preservation of "... safe, affordable and appropriate rental housing." However, legislation was needed to enable the City to prevent conversion of rented strata units to occupation by owner. The provincial government amended local government legislation so that local governments like the City could pass bylaws affecting the permissible tenure for accommodation. The means by which this can be done is to introduce zoning bylaws that limit the form of tenure within a zone or part of a zone. There is provision to protect legal non-conforming use, but the requirements to fall under this protective legislation did not apply to the units in the Six Buildings.

The City enacted a bylaw that limited the form of tenure for units in designated buildings (including the Six Buildings) to tenancies governed by a tenancy agreement that complies with the *Residential Tenancy Act* of British Columbia. The owner of the Six Buildings filed a petition in the Supreme Court of British Columbia arguing that the City bylaw was *ultra vires*, illegal or void. The court disagreed.

In coming to its conclusion, the court considered the standard of review that applies to municipal council decisions following the Supreme Court of Canada decision in *Canada (Minister of Citizenship and Immigration) v. Vavilov* [*Vavilov*], 2019 SCC 65 and the British Columbia Court of Appeal decision in *1120732 BC Ltd. v. Whistler (Resort Municipality)*, 2020 BCCA 101 applying *Vavilov* to municipal council decisions. At paragraph 47, the court wrote that municipal council decisions are entitled to a deferential reasonableness standard of review and that the question to be addressed is whether the City could have reasonably interpreted the provincial legislation so as to give the City the power to restrict the form of tenure of the Six Buildings in perpetuity to residential rental tenure.

At paragraph 61, the court noted that "It is in the nature of zoning bylaws that they compromise the fee simple ownership rights to some extent ... If fee simple rights of landlords could not be attenuated by municipal bylaws, then the zoning power conferred by the [local government legislation] to regulate residential rental tenure would be meaningless."

At paragraph 70, the court wrote in part "The Legislature appears to have intended to empower municipalities to preserve their rental housing stock. That is exactly what

Bylaw 8123 accomplishes. The consequence is that owners of strata units in the Six Buildings who were renting their units when Bylaw 8123 came into effect must continue to make their units available for rent."

And at paragraph 72, the court said:

> [72] Under the City's interpretation of the *RRT Amendment Act*, Bylaw 8123 is accomplishing the precise aims of the legislation. It serves the remedial purpose of enabling the City to prevent an owner from converting a rented strata unit into a unit that is owner-occupied, thus preserving the City's stock of available rental housing. That purpose does impinge upon the property rights of owners. But that is what the legislation, reasonably interpreted, appears to have intended. It cannot be unreasonable for the City to have enacted a Bylaw that precisely accomplishes the Legislature's purpose. There is simply no validity to an attack on Bylaw 8123 as an unreasonable, but otherwise *intra vires*, bylaw.
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> [73] It has not been shown that the *LGA*, as amended by the *RRT Amendment Act*, could not reasonably have been interpreted so as to allow for the adoption of Bylaw 8123. The City council, as a democratically elected body, may reasonably have considered the Bylaw as an authorized method of pursuing its policy goal of maintaining rental housing stock. That decision is deserving of deference. I find no basis for overturning the bylaw.

For present purposes, the intricacies of the legal arguments for and against the validity of the *VIT* bylaw need not be canvassed. Suffice it to say that the court decision is one in a long line of cases that have upheld the authority of local government to 'downzone' property and to thereby cause the owner financial loss without compensation. It amounts to an individual having to give up something of value *gratis* for the benefit of the community and then entering into a challenging discussion with real property assessment and taxation authorities about highest and best use and diminished value at the next assessment and taxation cycle.

The valuation challenge is obvious. In markets such as are being experienced in the Greater Vancouver Area, the Greater Toronto Area and other urban areas in Canada, how does an appraiser accommodate the risk of local government intervention to safeguard rental residential stock, or preclude use change for existing industrial land, or create any other potential use restriction?

There is some judicial guidance as to when the risk of change should be taken into account in the valuation process.[5] But every case is going to be highly fact specific.

Closing

The Supreme Court of Canada has described a government's power of expropriation as such:

> 20 The expropriation of property is one of the ultimate exercises of governmental authority. To take all or part of a person's property constitutes a severe loss and a very significant interference with a citizen's private property rights. It follows that the power of an expropriating authority should be strictly construed in favour of those whose rights have been affected...

Contrast the expropriation approach to downzoning under the exercise of police power. In the latter instance, and as noted above, local government decisions are to be treated deferentially applying a reasonableness standard that will override the safeguarding of individual rights. We have in stark contrast the government's ability under its police power to strip property owners of their property rights without compensation in pursuit of that government's vision of what is best for the public good.

There always has been and there always will be a conflict between the individual property rights of real property owners and governments bent on implementing policies perceived to be for the common good. With this conflict comes the question of the degree to which communities should benefit at the expense of individual property owners forced to relinquish property rights without compensation. Beyond the moral and philosophical issues, the conflict raises the challenge for the appraisal profession to accurately quantify the risk of downzoning without compensation and to reflect that risk in an opinion of market value of the fee simple interest.

End notes

1. The Appraisal Institute of Canada (Larry Dybvig, editor), *The Appraisal of Real Estate*, 3d ed., Vancouver: Sauder School of Business, 2010, p. 6.1
2. *Toronto Area Transit Operating Authority v. Dell Holdings Ltd.*, [1997] 1 S.C.R. 32 [*Dell*], at para. 22
3. See *Canadian Pacific Railway Co. v. Vancouver (City)*, 2006 SCC 5 for a discussion of *de facto* expropriation.
4. *The Appraisal of Real Estate*, p. 6.13
5. See for example *Petro-Canada Inc. v. Assessor of Area #12 – Coquitlam* 1991 CarswellBC 275 (B.C.S.C.); leave to appeal dismissed 1992 CarswellBC 1146 (B.C.C.A.) and cases judicially considering this case.

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