File No. 1629
Board Order No. 1629-1

November 12, 2010

SURFACE RIGHTS BOARD

IN THE MATTER OF THE PETROLEUM AND NATURAL GAS ACT, R.S.B.C., C. 361 AS AMENDED

AND IN THE MATTER OF
East ½ of Section 27, Township 26, Peace River District
except Plan H663

(The "Lands")

BETWEEN:

Burnem Hollister Grant
And Gertrude Grant

(APPLICANTS)

AND:

Murphy Oil Company Ltd.

(RESPONDENT)

BOARD ORDER

Heard:	September 15, 2010 at Fort St. John, BC
Panel:	Cheryl Vickers
Appearances:	Burnem Grant and Gertrude Grant, on their own behalf
	Rick Williams, Barrister and Solicitor, for the Respondent

INTRODUCTION

[1] The Applicant landowners, Burnem and Gertrude Grant, and the Respondent, Murphy Oil Company Ltd, (Murphy Oil) entered into two statutory right of way agreements, dated September 11, 2009, allowing Murphy Oil access to properties owned by the Grants (the Lands) for the purpose of constructing and operating two flowlines. The parties agreed to lump sum compensation for the use of the rights of way and for the compulsory aspect of the taking. The parties further agreed to submit a claim by the Grant's for additional compensation to account for diminishment in value of the Lands resulting from the rights of way and presence of the flowlines to the Board for determination. As the parties could not agree to a resolution of this claim, it was scheduled for arbitration.

ISSUE

[2] The only issue is whether compensation is payable by Murphy Oil to the Grants for diminution in value to the Lands, sometimes referred to as "injurious affection", and if so, how much is payable.

FACTS

[3] The Lands comprise 292.54 acres divided by Highway 2 and the Old Edmonton Highway (collectively the Highways). The Lands are zoned A-2 Large Agricultural Holdings and are designated "Agricultural – Rural Resource" by the Dawson Creek Rural Area Official Community Plan. The portion of the Lands lying east of the Highways (the East Portion) is approximately 36.4 acres and meets the Peace River Regional District Zoning By-law criteria for subdivision as a stand alone parcel. All of this area is within the Agricultural Land Reserve (ALR). Of the remaining 256.14 acre portion of the Lands to the west of the Highways (the West Portion), 115.35 acres is outside of the ALR and 140.79 acres is inside the ALR. Both the East and West Portions have access from Highway 2 and from the Old Edmonton Highway.

[4] The Grants operate a bison ranch approximately 16 kms from the Lands. They purchased the Lands in 2002 for speculative purposes. For the last eight years, the Lands have been farmed. The East Portion has Class 4 soil and is used to grow alfalfa. The West Portion has Class 4 and 5 soils and is partially cleared and cultivated, and partially forested. There is a residence, occupied by tenants, and farm buildings, some of which are in a dilapidated condition, on the

West Portion. A silo on the West Portion holds a wireless transmitter that provides high speed internet to the area.

[5] The rights of way for the two Murphy Oil flowlines are 18 metres wide and comprise, collectively, 6.37 acres. The first flowline right of way comprises 0.17 acres in the East Portion at the very northeast corner of the Lands along the northern edge of the property line, and connects with a wellsite located on the adjacent half section to the north. The second flowline right of way comprises 6.2 acres. It extends from the northern boundary of the Lands, in the East Portion, south along the eastern boundary, cuts across the Lands to cross under the Highways at a 90 degree angle, extends west across the West Portion to the western boundary, and continues south along the western boundary until turning west again into the adjacent half section. All but a small section of this right of way at the most southern part of the extension along the west boundary is located in that part of the Lands within the ALR.

[6] The flowlines in the rights of way carry sour gas. They are licensed to carry 2% hydrogen sulphide (H2S) but actually carry approximately 0.2% H2S. The residence on the Lands falls within the Emergency Planning Zone (EPZ) regulated by the Oil and Gas Commission (OGC). The occupants of the residence are subject to Murphy Oil's Emergency Response Plan, which provides protocol to be followed in the case of an emergency including provisions for shelter-in-place and evacuation.

[7] The flowlines are buried to a minimum depth of 1.5 metres. The land above the flowlines within the rights of way can continue to be used for agricultural purposes.

[8] Over the years, the Grants have considered filing an application with the Peace River Regional District (PRRD) to subdivide the East Portion from the Lands. They have gone so far as to fill in an application form and to speak with staff at the PRRD, but have not actually made an application for subdivision. They have received verbal advice from a staff person at the PRRD that subdivision of the East Portion from the rest of the Lands is viable. If the subdivision is approved by the PRRD, a separate application must also be made to the Agricultural Land Commission (ALC) for subdivision approval. Removal from the ALR requires a separate application to the ALC.

[9] The presence of the flowlines does not legally prevent subdivision of the Lands.

EVIDENCE AND ANALYSIS

[10] Pursuant to the *Petroleum and Natural Gas Act*, a landowner is entitled to be compensated for loss arising from the entry, occupation or use of land for the purpose of exploring for, developing or producing petroleum or a natural gas. If

the construction and operation of Murphy Oil's sour gas pipeline on the Grants' Lands causes loss to the Grants, Murphy Oil is liable to compensate for that loss.

[11] The compensable loss must be actual or reasonably foreseeable and proved on a balance of probabilities. Murphy Oil is not liable to compensate for possible or speculative loss in advance of a loss being probable.

[12] The Grants' claim for injurious affection, or loss in value to the remaining Lands, as a result of the rights of way and presence of the flowlines, arises in two ways. First, they say that the presence of the rights of way and flowlines on the East Portion has changed the highest and best use of the East Portion, making its subdivision from the Lands no longer probable, thus reducing its value. Second, they say that the market value of the West Portion is diminished because of the EPZ.

[13] To substantiate these claims, the evidence must demonstrate, on a balance of probabilities, that the value of the Lands, or each portion of the Lands, was greater before the signing of the rights of way and construction of the flowlines than after. Both parties called appraisal evidence. Anne Clayton, AACI, provided a summary report on behalf of the Grants providing an opinion of the loss of value to the Lands as a result of the flowline rights of way. John Wasmuth, AACI, provided an appraisal report appraising the market value of the area of land covered by the rights of way on a per acre basis, and providing an opinion about injurious affection to the rest of the land.

[14] I will address each claim in turn.

The East Portion

[15] Both appraisers provided an opinion with respect to highest and best use, although they approached the question from different perspectives and using different assumptions.

[16] Highest and best use is an appraisal concept that is described as the reasonably probable and legal use of a property that is physically possible, financially feasible and results in the highest value. The market value of property is based on its highest and best use. A determination of the highest and best use of property, or the use that will dictate a property's market value, involves consideration of what is physically possible, legally permissible, financially feasible and maximally productive.

[17] Ms. Clayton provided an opinion for the highest and best use of the East Portion as if it was a subdivided parcel. In her opinion, the highest and best use of the East Portion prior to construction of the flowlines was for development to a use permitted by the A-2 zoning such as a dwelling or dwelling with a home based business employing up to four employees. She did not do a highest and best use analysis to support this opinion.

[18] Based on the opinion that highest and best use of the East Portion was for subdivision and development, Ms. Clayton estimated the market value, as of August 2009, of the East Portion as a subdivided 36.4 acre parcel would have been $47,300 based on a price per acre of $1,250. In Ms. Clayton's opinion, the way the flowline cuts through the East Portion of the Lands would make a home business use permitted within the ALR difficult. In her opinion, the presence of the flowline rights of way in the East Portion significantly reduces the utility of the site so that its highest and best use is no longer development of a home site in conjunction with a home business, but is its current agricultural use as part of a larger farming operation. In Ms. Clayton's opinion, the value of agricultural land is $650/ acre based on sales of quarter sections in the area. Accordingly, she quantified the loss in value to the East Portion at $29,100 as follows:

Before flowline value	36.4 acres x $1,250/acre	$47,300
After flowline value	36.4 acres x $650/acre	$18,200
Difference in value		$29,100

[19] Mr. Wasmuth provided an opinion with respect to the whole half section. His highest and best use analysis led him to conclude that the highest and best use of the whole half section as of September 2009 was continued agricultural use given the overall agricultural soil capability, topography, ALR status, current zoning, location and permitted use. He recognized the property has the potential long term future use of subdivision of the East Portion for development as a country residential lot, however, considered such subdivision and development speculative at the time the rights of way were signed. In Mr. Wasmuth's opinion, the rights of way and installation of the flowlines did not change the highest and best use of the Lands. In his opinion, the highest and best use was for agricultural purposes before the rights of way agreements and construction of the flowlines, and continues to be so after construction.

[20] Mr. Wasmuth indicated he had reviewed ALC decisions with respect to small parcels with Class 5 and 6 soils and did not note any consistency in their determination of whether or not to allow subdivision. Murphy Oil provided three examples of decisions by the ALC North Panel denying applications for subdivision of land with Class 4, 5 or 6 soils. In all of these decisions, the Panel expressed some concern that allowing subdivision of small parcels would promote applications for exclusion from the ALR down the road, and would not encourage agricultural use of land within the ALR.

[21] Mr. and Mrs. Grant took issue with Mr. Wasmuth's conclusions of highest and best use and that the potential for subdivision and development is speculative. Their evidence was that there are considerable pressures on agriculture in the area these days and that it is not the most profitable and economic use of the property. They said there is demand for small land holdings or acreages to be used as residences or small businesses to service oil and gas activities. The Class 4 and 5 soils are limited in their productivity. Both the East

and West Portions have access and can be easily serviced with natural gas, power, telephone, high speed internet, water and sewer. They have observed other properties in the Dawson Creek area being rezoned and excluded from the ALR. They pointed to the recent purchase of property by an oil and gas company for establishing an office and yard site as an example of market activity indicating financial feasibility for subdivision. This transaction is one of the sales referred to by Ms. Clayton in estimating the value of the East Portion as if subdivided.

[22] The Grants provided an extract from the ALC's Annual Report for 2008-2009. This evidence indicates the ALC's North Panel received 118 applications in the year: eight for exclusions, eight for inclusions, and 102 for non-farm use and subdivision. Of the exclusions, 117.7 hectares were refused and 1,006.6 hectares were approved. Of these excluded hectares, 187.1 were prime land and 819.5 were secondary land. Consequently, the Grants consider it probable that an application to the ALR to exclude portions of the Lands from the ALR would be successful. The same exhibit indicates 1,430 hectares were approved for inclusion in the ALR. It does not indicate how many of the non-farm use and subdivision applications were approved or rejected.

[23] While both appraisers agree that the East Portion meets the zoning criteria for subdivision, they disagree on the probability that subdivision would ultimately be approved. Ms. Clayton's estimate of market value for the East Portion assumes its subdivision. Mr. Wasmuth considers the possibility to be just that, a future possibility, but is of the opinion that the market conditions do not exist at present to make subdivision and development of the East Portion profitable, feasible or probable. Reviewing the evidence of the probability of subdivision, I am not satisfied that it tips the scale from legally possible into probable. The Official Community Plan designates the Lands for agricultural use. One of the stated objectives of this designation is to assist the ALC in the preservation of lands in the ALR for agricultural purposes. Although the East Portion meets the criteria for subdivision in the zoning bylaw, that in itself does not mean an application would necessarily be approved. Even if it is approved, a further application must be made to the ALR and the evidence falls short of demonstrating that, in all probability, such an application would be approved. The excerpt from the ALC Annual Report shows that in 2008-2009 the North Panel approved for inclusion into the ALR more land than they approved for exclusion, for a net gain of land in the ALR. It does not indicate how many of the 102 applications for subdivision were approved. I have examples of three decisions from the North Panel of the ALC denying applications for subdivision of land with similar soil class and expressing concern that subdivision of small holdings does not support the purposes of the *Agricultural Land Commission Act*. So while I agree it was certainly possible that the East Portion could have been approved for subdivision before the rights of way agreements were signed, I am not satisfied that, as of that time, such approval was more likely than not.

[24] Turning to the market evidence, I am not satisfied that it demonstrates a demand for smaller subdivided parcels. Ms. Clayton provided four indices of

market activity for smaller acreages to support her estimate of value for the East Portion as if subdivided. Two are sales that occurred in 2005 and 2006, and are therefore, not indicative of market activity around the time the rights of way were signed. One is a current listing, not a sale. The fourth index, and the one referred to by the Grants and on which Ms. Clayton places most weight, is a 2010 transaction where the purchaser, an oil and gas company, agreed to pay the cost of rezoning and subdivision. However, rezoning and subdivision have not yet been approved. If the subdivision and removal of this parcel from the ALR is approved, and the sale completes, the sale may provide an indication of value for the East Portion if subdivision was approved, but as of the time both before and after the rights of way agreements were signed it only provides evidence of what might be possible.

[25] Mr. Wasmuth's evidence is that in the last three years there have only been two sales within a 15 kilometre radius of the Lands between 9 and 80 acres in size, and that there are numerous severed parcels in the area that remain under the same ownership as the parent parcel. The market evidence before me, therefore, does not demonstrate a demand for subdivided parcels.

[26] While I agree that subdivision of the East Portion was legally permissible, I am not satisfied the market conditions existed at the time the rights of way agreements were signed to make subdivision either probable, or feasible and maximally productive, and therefore its highest and best use. The evidence convinces me that the highest and best use of the Lands including both the East and West Portions was and is continued existing agricultural use.

[27] In any event, even if the highest and best use of the East Portion was for subdivision as of the time the rights of way were signed, the presence of the flowlines does not render the East Portion un-subdividable. The flowline does not affect the qualifications for subdivision under the zoning by-law. The same possibility of subdivision of the East Portion exists today, after installation of the flowlines as it did before installation of the flowlines. The flowlines do not render the East Portion, if subdivided, unusable for development. The evidence is that even considering set backs from the rights of way, the property will contain building sites capable of supporting allowable uses under the zoning bylaw. Nor is there evidence that presence of the flowlines necessarily changes the likelihood of approval of a subdivision by the PRRD or removal of the land from the ALR by the ALC. These steps to development remain in place and the evidence does not disclose that the likelihood of approval is any less as a result of the flowlines.

[28] Mr. Grant agreed that there is nothing legally preventing the subdivision of the Lands because of the flowlines, but argued that the subdivided parcel would be less desirable. There is no market evidence to support that argument. The Board cannot award compensation based on a hunch or a feeling of loss. The loss must be supported by evidence.

[29] I find that the highest and best use of the East Portion is, and was before the rights of way agreements were signed, its continued agricultural use for the time being and that the possibility of subdivision and alternate use of the East Portion has not changed as a result of the rights of way and flowlines. I am not satisfied the market value of the East Portion has diminished as a result of the rights of way agreements and flowlines. Consequently, there is no basis for compensation for injurious affection.

The West Portion

[30] The claim of injurious affection for the West Portion is based entirely on the presence of the EPZ and the argument that being in the EPZ negatively affects the value of the Lands. Ms. Clayton's opinion is that market value has been reduced by 10-25% as the occupants of this site are subject to the provision of the Emergency Planning Zone (EPZ).

[31] To calculate loss, Ms. Clayton provided three sales of residential acreages from 59.3 acres to 639 acres, occurring in 2008 and 2010, and indicating a range of value from $375,000 to $422,000. Placing most weight on the sale of a 59.3 acre site with a 27 year old, 2,884 square foot home with a guest cabin and greenhouse selling in June of 2008 for a time adjusted price of $422,000, she estimated loss of value for the West Portion to be in the range of $42,000 (10% of $422,000) to $105,000 (25% of $422,000).

[32] Ms. Clayton conceded that she is not aware of any studies that support her conclusion of diminution in value and that there is no market evidence to support a reduction to market value for being within an EPZ. She admitted to being unaware of any studies demonstrating that the value of land is negatively impacted by the presence of a pipeline or as a result of being inside an EPZ. Nor is she aware of any pattern of dealings that includes compensation for being in an EPZ.

[33] Mr. Wasmuth reported that he conducted a literature search on injurious affection. He indicated that while pipeline rights of way acquired through residential subdivisions have in some instances been found to negatively affect market price, he was not aware of any North American studies that indicate any negative impacts on market prices for agricultural holdings as a result of pipeline rights of way. In his own appraisal experience, he has never found a correlation to indicate a negative impact on the market prices of agricultural properties that contain underground pipelines.

[34] In the Grants' view, the diminishment of value comes from the fact that the flowline crosses the middle of the Lands rather than following property boundaries. In their view, the impact on the value of the Lands would have been much less if the flowlines had followed the property lines. There is no evidence, however, that the location of the flowline affects the continued use of the West Portion for agricultural purposes.

[35] There is simply no market evidence to support the claim for injurious affection to the West Portion. Neither appraiser could provide market evidence or studies to support diminishment of land value for the presence of a buried pipeline. If the presence of underground pipelines negatively affects the value of agricultural land, that impact should be evident from sales. As indicated above, the Board cannot compensate for loss based on a hunch or belief. The alleged loss must be supported with evidence and proved on a balance of probabilities. I find the evidence falls far short of demonstrating a negative impact to the value of the West Portion as a result of the rights of way and flowline or the EPZ, and consequently there is no basis for compensation for injurious affection to the West Portion of the Lands.

CONCLUSION

[36] I find that the probable use of the Lands into the foreseeable future has not changed as a result of the rights of way and flowlines and that the evidence does not demonstrate that the value of the Lands is less today as a result of the rights of way and flowlines than it was before the rights of way agreements were signed. Consequently, I find no compensation is payable by Murphy Oil to the Grants for injurious affection to the Lands.

DATED November 12, 2010

FOR THE BOARD

Cheryl Vickers, Chair