VALUATION CASE STUDY
PAPER MILLS

The Challenge

Our client, faced with paying almost $5.0 million in property taxes annually on their paper mill complex, questioned whether its $116 million realty assessment was reasonable. They turned to Turner Drake for advice.

Turner Drake's Approach

The 300 acre site accommodated two of the most modern paper mills in the world, a Kraft mill, experimental plant and recovery boiler: almost two million square feet of space spread over 40 buildings. Lee Weatherby, the senior valuer assigned to the assignment, confessed to a twinge of doubt as the mill complex reared up out of the fog. Fortunate then that we had budgeted him an assistant. Rolling up their sleeves they got to work inspecting, measuring and cataloguing every brick and stick. Provincial legislation mandated that only the real estate was assessable; plant, equipment and machinery that was part of the manufacturing process had therefore to be excluded … an exercise not entirely devoid of challenge given that the buildings were purpose designed, and frequently integrated with the manufacturing process they housed. As part of their visit our valuation team interviewed on-site management and mapped out the manufacturing process to identify which elements of the heating, electrical, water, sewage disposal and building re-inforcement were dictated by it, rather than the real estate. This assisted them determine the taxable realty. Although there are potentially three methods for calculating Market Value (the basis for the realty assessment) valuation of Special Purpose Property such as paper mills, is usually reliant on the Cost Approach. This method involves first computing the Replacement Cost New (RCN), deducting therefrom the Physical, Functional and External Obsolescences and then adding the outcome to the land value (ascertained by reference to the sale prices of comparable sites). Calculating the RCN is a relatively mechanical process using costing software. Physical Obsolescence (depreciation) is a function of the building's age and maintenance. Accurately ascertaining Functional Obsolescence however requires an in-depth understanding of the manufacturing process. We understand the difference between job shops and machine paced assembly lines, batch flows and continuous flows but the only way to properly comprehend the process is to interview the production managers. How does the current building design facilitate or impede the production flow? Are ceiling heights adequate … or over adequate? What about the capacity and reliability of power supply, water and effluent disposal? Is the facility layout optimum? Are there adequate ancillary and storage faculties? Does the site configuration assist or constrain materials handling and truck loading? External Obsolescence, the loss in value due to economic factors, can also be *very* significant for a Special Purpose Property. Is there a pool of skilled labour available locally? If not, who bears the cost of training and education; the Province or the employer? Where are the markets for the products? How do they get there? How well positioned is the facility to handle competition from emerging suppliers in South America, India and China? How sensitive is the product to fluctuations in the Canadian dollar? What is the likely impact of new, disruptive technologies such as the Internet or new manufacturing processes? This required an analysis of the market segment: with single use property the value of the real estate is function of the viability of the business enterprise it accommodates.

Winning Results

Turner Drake furnished the client with "court ready" Master Valuation Report, on-going expert assistance, including negotiations of the property tax appeal, resulting in a major reduction in the realty assessment.

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