Law Reform Commission of British Columbia
Report on Discount Rates

This Report took the form of a letter to the Chief Justice of the Supreme Court and was published as Appendix to the Commission's 1980 Annual Report (LRC 49)

Appendix C

TEXT OF COMMISSION'S LETTER CONCERNING DISCOUNT RATES

November 18, 1980

The Honourable Allan McEachern
Chief Justice
Supreme Court of British Columbia
The Law Courts
800 Smithe Street
Vancouver, B.C.
V6Z 2E1

Re: Discount Rates

Dear Chief Justice:

Thank you for your letter of November 4th. Coincidentally the matter of discount rates was discussed by the members of the Law Reform Commission at its meeting on November 3rd. The sense of urgency in your own letter and the gist of our own discussions suggest that the Commission's involvement in this matter should draw to a close.

The issue of discount rates was first referred to the Commission in a letter from the Deputy Attorney General in February of this year. That letter enclosed a copy of a draft *Prospective Pecuniary Damages Act* dealing, *inter alia,* with discount rates and indicated that you had a special interest in it. Mr. Vogel requested the Commission to "assess this proposal and make constructive comments" and it was in that spirit the Commission approached it. The primary task was seen as providing what assistance we could to you and the Ministry of Attorney General rather than undertaking this as a full-fledged Commission project, with a fully researched working paper circulated for comment culminating in a formal report setting out final recommendations.

In April the Commission wrote to the Attorney General suggesting an amendment to the *Supreme Court Act* along the following lines:

The Chief Justice, after consulting the other judges of the court and such other persons as he considers appropriate, may prescribe from time to time the rate of interest to be used in determining the capitalized value of an award in respect of future damages.

This suggestion prompted further discussion which largely centred on two principal issues:

1. Should the discount rate be set by a person or body other than the Chief Justice (S.C.B.C.)?
2. Should the discount rate prescribed be limited to one that reflects only the difference between the estimated rates of price inflation and investment or should the so-called "productivity factor" be an additional parameter?

On the first issue, the Commission adheres to the view expressed in the April letter: the Chief Justice, after such consultation as he may think necessary, is the appropriate person to set the discount rate. I should add, however, that the Commission has no reason to oppose the rate being set by a small committee of judges consisting, say, of the Chief Justice and two puisne judges. The Commission's view is that it is important that the determination of a discount rate be done by a judge or by a committee of judges. The determination of a discount rate or rates to be used in making damage awards is now an independent judicial function. This important independent quality of the function is preserved if setting of a discount rate or rates of general application is made by the Chief Justice or by a committee of judges. We do not think it appropriate that the function be performed by either the Legislature or by the Executive, on authorization by the Legislature, because of the close identification in interest of Government and the Insurance Corporation of British Columbia which pays the vast majority of the damage awards in personal injury cases made by the Courts of this Province. For example; the determination of a high discount rate by Act of the Legislature or authorized act of the executive branch of Government would quite likely be construed by some as politically motivated in order to save money for the Insurance Corporation.

The second issue is a more subtle and difficult one. As a starting point it might be useful to define what we understand to be the "productivity factor."

The economic information that we have received suggests, as do the cases in which this factor has been noticed, that owing to advances in technology and the like our society as a whole is becoming more productive in terms of the number of units of goods and services produced per citizen. The benefits of this increased productivity accrue, in part, to all citizens in the form of increases in their earnings over and above those increases which simply reflect price inflation. It is this increase that we identify as the productivity factor. The economic information stresses that this benefit accrues to all income earners – even those employed in a particular industry where there is no identifiable increase in productivity. This benefit is also distinct from earning increases (or decreases) that may be identified with career advancement that depends on characteristics of the individual to be compensated or the identifiable occupational group to which he belongs.

This view of the productivity factor is based on a selective reading of cases and comment and on some consultation with a senior actuary. While we have no reason to doubt its accuracy, we cannot say with confidence that we have fully explored all the complexities associated with economic concepts of this kind.

Since the projected general rate of increase of earnings (including productivity factor) is greater than the projected rate of price inflation, it appears that it would be inappropriate to apply a discount rate determined solely with reference to the price inflation to determine the present value of future income losses. Clearly a second discount rate, one that reflects the productivity factor, should be used for this purpose. This second discount rate would be somewhat less than that used for non-income related future losses or expenses.

In Ontario, the enabling legislation appears to contemplate only a single discount rate and this was the view adopted by the Morden Committee in developing their "rule." The enabling provision, section 114(l0)(ba) of *The Judicature Act,* R.S.O. 1970, c. 228 *am.* SO. 1979, c. 65, s. *6(5),* provides:

> Subject to the approval of the Lieutenant Governor in Council, the Rules committee may make . . . rules . . . for
> (ba) prescribing the rate of interest to be used in determining the capitalized value of an award in respect of future damages.

The rule prescribed under that power reads as follows:

> The rate of interest to be used in determining the capitalized value of an award in respect of future pecuniary damages, to the extent that it reflects the difference between estimated investment and price inflation rates, is 2½ per cent per annum.

The options are to adopt the Ontario approach of providing for a single discount rate or to develop enabling legislation that would provide for the setting of two discount rates.

As we understand it, the object of fixing discount rates is twofold. First, it is meant to overcome the unfortunate face that is put on the administration of justice when the Courts reach disparate conclusions on the same facts. Since the setting of a discount rate is, essentially, a prophecy as to future economic events and unrelated to the facts of a particular case, inconsistent results from case to case are difficult to justify.

Secondly it is meant to eliminate the need to adduce repetitive and time-consuming economic evidence that is presently necessary to enable the Court to set a discount rate in individual cases. This imposes a significant financial burden on the parties to the litigation. Moreover the amount of Court time spent hearing the same evidence in numerous cases suggests the present practice causes a significant and unnecessary wastage of trial time.

How well does the Ontario solution serve the objects stated? As Mr. Justice Dickson of the Supreme Court of Canada recently pointed out:

the award of damages is not simply an exercise in mathematics which a judge indulges in, leading to a 'correct' global figure. The evidence of actuaries and economists is of value in arriving at a fair and just result. *(Lewis* v. *Todd,* October 28, 1980.)

If it is clear, as it is in Ontario, that the productivity factor is not taken into account in setting the single discount rate, expert evidence will still be of value to achieve a "fair and just result." The Court has a duty to hear, and the Ontario rule will not exclude, relevant and proper evidence concerning actual loss taking into account the productivity factor.. Thus a principal aim of a fixed discount rate(s) – relieving the Courts and the parties of the various burdens associated with evidence on general economic matters – is not fully served. Such evidence may be led whenever the potential increase in the award may justify it. Likewise the Ontario one-rate solution will not, in actions involving future loss of earnings, put an end to disparate results from case to case.

Even if a rate similar to that provided by the Ontario rule would be accepted in practice as applicable to loss of future income then, while the objects of fixing a discount rate are met, it is apparent that justice will not be well served and imperfect compensation will result. The two discount rate approach seems to offer a sharper tool for the rational assessment of future damages and is likely to yield more precise results in this difficult area.

Having regard to the way in which the matter of discount rates was referred to us, and the way in which we have approached it, we do not believe that it is appropriate to make a "recommendation" as such. The Commission prefers the two-rate approach, but, as the final decision may involve a measure of pragmatic considerations, we believe it should be left to be worked out between you and the Attorney General. What we have done is prepare draft legislation that embodies our preferred two-rate approach. This may provide a starting point for legislative action.

Whether the Ontario scheme or the Commission's preferred scheme is adopted, we think it is important to note that its success in achieving its aims will depend on what the Morden Committee Report referred to as "a discriminating judicial interpretation which is largely informed by an understanding of the purpose of the legislation."

I enclose our draft of an amendment to the Court Rules Act with drafting notes thereto. The Commission's statutory obligation is to report its views concerning changes in the law to the Honourable Attorney General. Accordingly, I am sending copies of this letter, the draft amendment and drafting notes to the Attorney and to his Deputy.

If there are any aspects of our views that you would like to discuss, I should be pleased to see you at any time at your convenience.

Yours truly,
The Hon. Mr. Justice J. S. Aikins
Chairman

DRAFT PROVISION

The Court Rules Act, R.S.B.C. 1979, c. 77 is amended by adding the following section:

Discount rates

4. (1) In this section
"discount rate" means the rate, expressed as a percentage, used in calculating the present value of future damages;
"future damages" means damages to compensate for pecuniary losses to be incurred or expenditures to be made after the trial of a proceeding.
[As to the definition of "proceeding" see drafting note 1, infra]

(2) The Chief Justice of the Supreme Court of British Columbia may from time to time prescribe:
(a) a discount rate which shall be deemed to be the future difference between the investment rate of interest and the rate of increase of earnings due to inflation and general increases in productivity, and
(b) a discount rate which shall be deemed to be the future difference between the investment rate of interest and the rate of general price inflation.
[As to "prescribe" see drafting note 2, *infra]*

(3) In any proceeding the discount rate prescribed under subsection (2) (a) shall be used in calculating the present value of future damages that are intended to compensate for or are determined with reference to
(a) loss of future earnings because of partial or total loss of income earning capacity, or (b) loss of dependency under the *Family Compensation Act,* and the discount rate prescribed under subsection (2)(b) shall be used in calculating the present value of all other future damages.
[N.B. Drafting notes 3 to 6 which are of general application and not specifically noted above.]

DRAFTING NOTES

1. "Proceeding" is defined in the *Supreme CourtAct* as "an action, suit, cause, matter, appeal or originating application."

Section 40(1) of the *Interpretation Act* provides that "the interpretation section of the *Supreme Court Act,* so far as the terms defined can be applied, extends to all enactments relating to legal proceedings."

Thus the definition would extend to this provision.

Quaere the application of the provision to an arbitration.

2. A rate "prescribed" under subsection (2) would seem to be caught by the general limb of the definition of "regulation" in the *Regulation Act:* "every regulation, rule, order, proclamation and bylaw of a legislative nature made under or by the authority of any Act.

Thus it would attract the provisions of the *Regulation Act* concerning filing and publication.

3. The draft is silent on the source of funds to be used by the Chief Justice in the discharge of his function (e.g. the cost of engaging experts to provide advice on economic and actuarial matters).

If no general fund is available an appropriate specific provision for funding should be made.

4. A potential addition to the list of future loss items to which the income discount rate should apply is future expenditures in the form of wages. An example would be that part of an award designed to provide a quadraplegic with the 24 hour services of an orderly.

Common sense suggests that the wages of an orderly will accelerate more rapidly than other future care items and that the discount rate used for income loss should apply. This view has been adopted in at least one B .C. case *(Bracey* v. *Johnson,* unreported, Vancouver Registry 44398l75, June 13, 1980, per Gould J. at p. 21 of the decision manuscript.)

The accepted economic view is that this is not an income related loss and it should be capitalized at the higher rate. This is the view reflected in the draft.

5. Implicit in the draft is the notion that general economic evidence is no longer relevant in the light of the "deeming" language of subsection (2), and that all evidence and valuation should be on a "constant dollar basis."

Quaere whether this should be made explicit in the draft. An earlier version of our draft contained the following provision.

In any proceeding in which a discount rate is applicable

(a) no evidence shall be admitted with respect to rates of inflation, rates of return on investments or increases in salary or wages resulting from inflation or general increases in productivity, either past or future, and
(b) all matters relating to future contingencies or prospects shall be expressed in constant dollars from which all elements of prospective inflation and prospective increases in earnings attributable to general productivity increases have been removed.

6. It will be noted that there is some divergence between the definition of "future damages" and section 2(a) of the *Court Order Interest Act* as to the point in time from which damages are to be regarded as future damages. This draft speaks of losses etc. arising after the "trial" while the *COIA* refers to the "date of the order." Where judgment is reserved these may be two different times.

Of the two, we believe the time of trial is, in principle, correct. This was the Commission's view in its Report on Prejudgment Interest and the COIA imperfectly implemented the recommendations in this regard. In practice, however, nothing turns on this error.