CHANGE OF USE TAX A BRIEF OVERVIEW

Change of use tax is a subject all too often overlooked by the Real-Estate practitioner when advising a purchasing client. Generally speaking it will be of primary concern to practitioners when advising clients on raw land\lot purchases. There are three classifications of assessment, in The Assessment Act R.S.N.S. 1989 c.23 (as amended) which in the normal course of events should alert practitioners to review the issue with their clients more fully, and these are;

- farm property (s.47)
- forest property (s.49)
- for want of a better term "non-profit property" (s.29).
-

Farm property

Farm property is defined in s.2(g) of the Assessment Act to mean,

> "the land and complementary buildings used for Agricultural purposes but does not include any residential property and the land used in connection therewith"

Section 46 subsection (1) of the Assessment Act exempts this classification of property from taxation, but there is a price exacted for this generous treatment by subsection (6) in the form of change in use tax. This tax is levied when " the land ceases to be used for agricultural purposes" and amounts to 20% of the property's assessed value.(subject to some exemptions common to farm and forestry property which will be dealt with later in this paper).

Most important to the client is that this change of use tax is constituted a lien on the land by subsection 46(8).

Forestry Property

Forestry property is also exempt tax pursuant to subsection 47(1) of the Act. The subsection states that

> "all property bona fide used or intended to be used for forestry purposes shall be exempt from real property tax."

Forestry property is defined by subsection 2(h) to include essentially all property not used

for residential, commercial or industrial purposes. . But once again should the forestry use cease then a change of use tax equal to 20% of the assessed value will be levied and the tax due will constitute a lien on the land.

Non Profit Property

Section 29 of the act exempts from taxation with

> "all land in excess of 3 acres of any non-profit charitable fraternal educational religious cultural or sporting organization excluding buildings and structures."

The section, however, imposes a per acre tax on the land and in addition levies a 50% change of use tax when the land ceases to be used for its original non-profit purpose. Similar to the other two sections of the Act this tax also constitutes a lien against the land.

Exceptions

In the case of Farm and Forest property there are exceptions to the general rule:

- If the new use is either Farm or forest property.
- If the land which ceases to be used for forest or farm purposes is sold as a building lot to an immediate family member and does not exceed one acre or the minimum size required by law.

Conclusion and Analysis

Ideally this issue should be discussed with the client before the Agreement of Purchase and Sale is signed. At that time the prudent practitioner should determine the assessment classification of the subject property and then find out from the client what the client's proposed use of the land is, in order to determine if there is a possibility that change of use tax might be levied.

The issue of liability for change of use tax was recently canvassed by the Supreme Court Appeals Division in the case of Eastern Forestry Resources Limited v. The Director of Assessment and Municipality of the District of Lunenburg (1991),108 N.S.R. (2d) 357. In rendering the decision of the court Matthews J.A. quoted from an earlier decision of MacDonald J.A. Green Meadows Estates Ltd v. Director of Assessment (1984), 64 N.S.R. (2d) 36 where he commented at p.39:

> "[14} Section 40A(6) (now s.46(6)) of the Assessment Act does not specify that the change-in-use tax shall be based on a new use of the property. The section simply says in effect that if farm property ceases to be used for agricultural purposes it is no longer exempt from taxation and a change-in-use tax is therefore payable. What triggers the change-in-use tax therefore, is not a new use of the land but rather the cessation of an existing one. The phrase 'change-in-use tax' is really not quite accurate; it is a tax rather for ceasing to use for farm purposes . It requires a new assessment to be made, valued at the time of the cessation of use. It is a tax additional to whatever tax has been or will be levied as a result of the normal annual classification and assessment to the land for the year in which cessation of use occurs or the normal tax for the following year.
>
> .....
>
> "[16] Such issues as whether there was any evidence of a substantial act indicating an intent to use the land as residential property or as to how the property should be classified when it has ceased to be used for agricultural purposes are really irrelevant. The question here for determination is not when did the property first become used for residential purposes; rather, the crucial question is when did the property cease to be used for agricultural purposes?"

After quoting this excerpt Matthews J.A. states,

> "the same reasoning applies to land which had been used for forestry purposes."

Thus it would seem that every case must revolve around its own facts. If the Vendor, as a farmer had gone out and obtained subdivision approval for a number of lots and had then advertised the lots for sale as building lots, then using the analysis of the Appeals Division, he as Vendor should be responsible for the change in use tax since its use as a farm property ceased when he obtained approval for the subdivision. If however the client had approached the Vendor and asked to purchase a lot off a farm or woodlot then it would seem that the use would cease when the purchaser acquired title. In between these two situations there are innumerable variations, each of which must be interpreted on its own facts.

What if the client, has, as is usually the case already signed the Agreement of purchase and sale when they first attend to provide instructions? There is still an onus on the

practitioner to determine the assessed classification of the land and enquire as to the intended use of the land. The framework of the analysis should still be the same and the question asked, "when did the property cease to be used for agricultural or forestry purposes? If there is a dispute, then as a matter of practicality, I would suggest that a speedy way of having it resolved would be to make an application under the Vendors and Purchasers Act.

One last area to be aware of is "the exception to the exception" when there is a sale of a building lot to an immediate family member! If that family member then resells the lot within seven years, of acquiring it the family member as transferor is liable for the change of use tax (see subsection 14 of section 46 and 47 of the Assessment Act. The warning signal for this should be the appearance of a statutory declaration in the Registry of Deeds which must be filed, whereby the transferor makes the original claim for exemption. Obviously if this is dated within seven years of the closing date the issue of change of use tax as an adjustment must be raised with the Vendor prior to closing.

The Purchaser and Property Insurance

When representing a Purchaser in a real property transaction involving land and buildings there are two insurable interests that need to be canvassed with the purchaser. Firstly the issue of insuring the purchasers' pre-closing interest in the property, and secondly the protection of the purchasers and the mortgagees interest in the property after the transaction closes.

Pre-closing interest of the Purchaser

Since the pronouncement of McKeigan C.J.N.S. in the case of Wile v. Cook (1983) 63 N.S.R. (2d) 14 where he stated, "Thus any knowledgable solicitor should always advise a purchaser to protect himself by putting a temporary cover on the property with his own insurer' there is now a responsibility on the purchasers' solicitor to recommend that the client obtain preclosing insurance Essentially the purpose of this is to cover the possibility that the Vendor does not have insurance in place in the event that the property which is the subject of the Agreement of Purchase and Sale is damaged or destroyed prior to the closing. This area of the law was well covered in a paper given by Paul B Miller, as Chapter 13 of the 1987 CLE Real Estate Seminar, entitled Insurance Clauses in Agreements of Purchase and Sale which I highly recommend to all as a detailed examination of this topic.

Proof of Insurance at Closing

It is very important to canvass with the client well in advance of the closing the necessity of having insurance coverage in place, particularly if the client has obtained financing from a commercial lending institution. Mortgage instructions don't appear to follow any set pattern in specifying how much Insurance should be put in place and a brief review of instructions recently received at our office revealed the following.

- Instructions from Scotia Mortgage Corporation direct that a specific amount of insurance be in place
- Instructions from CIBC and The Toronto Dominion Bank require coverage in at least an amount equal to the replacement value of the building.
- Instructions from Royal Bank of Canada require coverage in the lesser of the amount of the mortgage or the insurable value of the building.

So while it may seem trite to mention it **read the instructions**.

Even if there is no mortgage being put in place, it is prudent to recommend to the client that they consider placing insurance on the buildings and structures.

It is of course a standard part of a commercial lenders instructions that the mortgagors

solicitor obtain proof of insurance and ascertain that the policy contains the standard Mortgage Clause endorsement before advancing any funds on the mortgage. Often, however in the rush to close, the binder that is faxed over does not contain confirmation that the Standard Mortgage Clause applies to the insurance. It is important to ensure that this clause is specifically mentioned in the binder, because sub-clause 1 of the Standard Mortgage Clause states that,

> "this Insurance, as to the interest of the Mortgagee only therein, is and shall be in full force **notwithstanding anything contained in or omitted from the application for insurance**, and **shall not be invalidated by any act or neglect of the Mortgagor, owner or tenant of the property insured**, **nor by the occupation of the premises for purposes more hazardous than are permitted by this policy, nor by non-occupation .....**" (emphasis added/a full copy of the clause is appended to this paper)

Failure to ensure that the Banks instructions are carried out in full could result in exposure to potential liability if the policy is rendered void by any of the circumstances set out above.

In Pictou County it is the practice that most of the Insurance Agents attach the Standard Mortgage Clause to the policy as soon as they place the Mortgagee on the policy as "loss payable to", but all too frequently there is no confirmation of this on the Binder that is sent along prior to closing. Funds should not be advanced unless and until a Binder, in a form similar to that attached as Appendix ii has been issued, indicating a binding obligation to provide insurance. Without this document there is no way of fulfilling the Banks' instructions, e.g. the purchaser may not pay the insurance agent; the amount of coverage may not be sufficient or the policy may not contain the Standard Mortgage Clause amongst other things.

Assured

Mortgage No.

MORTGAGE CLAUSE INSURANCE ENDORSEMENT

GRANTED TO

THE TORONTO-DOMINION BANK

HEREIN CALLED THE MORTGAGEE, THE INSURER BEING CALLED THE COMPANY

It is hereby provided and agreed:

1. That this Insurance, as to the interest of the Mortgagee only therein, is and shall be in full force notwithstanding anything contained in or omitted from the application for insurance, and shall not be invalidated by any act or neglect of the Mortgagor, owner or tenant of the property insured, nor by the occupation of the premises for purposes more hazardous than are permitted by this policy, nor by non-occupation, it being contemplated that as between the Company and the Mortgagee, the Local Agent of the Company procure all information which the Mortgagee may be unable to furnish relating to the property insured.

2. That whenever the Company shall pay the Mortgagee any sum for loss under this Policy, and shall claim that as to the Mortgagor or owner no liability therefor existed, the Company shall thereupon be legally subrogated to all rights of the Mortgagee under all the securities then held as collateral to the mortgagee debt to the extent of such payment, but such subrogation shall not impair the rights of the Mortgagee to recover the full amount of its claim; or at its option, the Company may pay to the Mortgagee the whole principal due or to become due on the mortgage with the interest then accrued and shall thereupon receive a full assignment and transfer of the mortgage and all other securities held as collateral to the mortgage debt.

3. That in case of loss or damage by fire or other perils insured against, the Mortgagee shall be entitled to receive payment of the amount of such loss or damage, if they shall, on the same coming to their knowledge, give notice thereof to the Company, and within a reasonable time thereafter deliver an account of the loss or damage as particular as the nature of the case will admit of, and make proof of the same by declaration or affirmation, and produce such other evidence as the Directors of the Company may reasonably require, and such payment shall be made within sixty days after the delivery of such account

4. That this Policy, as between the Company and the Mortgagee, shall continue in force so long as any of the money secured by the mortgage is unpaid, notwithstanding that the time of payment of premium or renewal premium may have elapsed, until either the Company or the Mortgagee give ten days' notice in writing to the other of them of their desire that the Policy shall no longer continue in force.

5. That this Policy cannot be cancelled by the Assured without the written consent of The Toronto-Dominion Bank.

6. The insurer will neither terminate nor alter the policy to the prejudice of the Mortgagee without the prior written consent of The Toronto-Dominion Bank.

7. Further Insurance permitted without notice until required by the Company

At the request of the assured the loss, if any, under this Policy, is hereby made payable solely to The Toronto-Dominion Bank, as Mortgagee, subject to the conditions of the above "Mortgage Clause"

Attached to and forming part of Policy No. *of the*

Issued at its *Agency.*

Date

4200B(12-85)

Authorized Representative

__New Renewal of Binder No. Extension of Policy No. 5263686

Name of Insured and Address:	PURPOSE OF BINDER - This Binder is a temporary insurance contract to serve a evidence of Insurance:
Louis J. Kiley & Carol Ann Cole P. O. Box 579 New Glasgow, Nova Scotia B2H 5L4	__ Pending Issuance & Delivery ofPolicy __ Pending Issuance & Delivery of a Renewal Policy XX Pending Issuance & Delivery of Endorsement to Policy __ Pending Negotiations of Rates, Premium or Coverage
Business or Occupation:	

The Dominion Insurance Corporation
(Name of Insurance Company)

is hereby bound to an insurance undertaking for the Insured named above subject to the conditions set forth as follows:

DESCRIPTION OF AUTOMOBILES, PROPERTY OR OPERATIONS AND LOCATIONS.	TYPE OF INSURANCE COVERAGE AND INSURED PERILS	AMOUNT OF INSURANCE OR LIMITS OF LIABILITY
Family home located at Abercrombie	All Risk on building. Legal liability THE POLICY CONTAINS A CLAUSE THAT MAY LIMIT THE	$ 268,000 $1,000,000 AMOUNT PAYABLE.

MORTGAGEE OR LOSS PAYEE, Loss, if any, is payable to insured and:	The following clauses, special conditions or endorsements shall apply to this insurance.
Royal Bank of Canada Provost Street New Glasgow, Nova Scotia B2H 2P5	$1000 deductible Standard mortgage clause.

ORIGINAL BINDER SENT TO: __ Insured __ Mortgagee or Loss Payee XX Other

Mac, Mac & M

In consideration of the Insured's agreement to pay a premium based on published or manual rules and rates, and subject to all the provisions of the policy customarily issued in the province where the insured property is situated, or exposures exist, by the Company bound herein insuring against the perils or the coverages specifically designated, it is agreed th insurance of the type named above is bound for the following period:

From Mar. 30, 1994 at 02:00 p.m. to Apr. 30,1994 at __ Noon
XX 12:01 a.m.

Standard time, or such time prior thereto as the Company's policy may be issued in lie hereof insuring the described risk. A premium charge shall be made for the term of this Binder, calculated in the manner provided above, unless a policy is issued by this Company a is accepted by the Insured covering the Binder term. The issuance of such a policy shall vo this Binder.

Date: March 30, 1994 By: Marie Lapierre
Authorized Representative or Agent

TOTAL P.02