

BETWEEN:

JAMES M. McLEAN ..... APPELLANT;

AND

THE MINISTER OF NATIONAL }  
REVENUE ..... } RESPONDENT.

Toronto  
1965  
} Dec. 6  
Ottawa  
Dec. 16

*Estate tax—Estate Tax Act, S.C. 1958, c. 29, ss. 3, 5(1)(a), 58(1)(o) and (s)—Valuation of leasehold interest—Possibility of leasehold interest having no value, a plus value, or a minus value—Rent payable vs. economic rent.*

At his death the deceased was a tenant under a written lease that still had 26 months to run at a monthly rental of \$300 and his estate sought to deduct the full liability therefor, or \$7,800, as a debt of the estate.

The Minister, on the other hand, while agreeing to allow this deduction, sought to add the sum of \$4,340 as the value of the unexpired term of the lease in the absence of any obligation to pay rent.

*Held:* For the purpose of the *Estate Tax Act*, R.S.C. 1958, c. 29 as amended, a leasehold interest as an item of property has no market value when a tenant is paying pursuant to his lease contract the full rental value that the property is worth that is the economic rental; when a tenant is paying less than the economic rent his leasehold interest as an item of property has a plus value; and when a tenant is paying more than the economic rental it has a minus value; and it is the amount of the burden of a leasehold interest on an estate that has to be assessed and allowed to be deducted from the value of the deceased's estate before determining the balance on which the Estate Tax is payable; and this can be done in two ways, namely, by doing it the way the Minister has, or by valuing it on a net basis, either of which way the same result obtains.

2. That the appeal be dismissed.

APPEAL from a decision of the Tax Appeal Board.

*M. C. McLean* for appellant.

*D. G. H. Bowman* for respondent.

GIBSON J.:—This is an appeal from a decision of the Tax Appeal Board dated November 13, 1964 in respect of the

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estate tax assessment dated March 26, 1964 of James M. McLean executor under the will of Charles Harold Jaimet of the City of Hamilton in the County of Wentworth.

The issue in this appeal is the determination of the true computation of the aggregate net value of the property passing on the death of this deceased in so far as such property relates to a lease of premises situate at 65 Markland Street, Hamilton, Ontario.

Among the facts agreed to by the parties are the following:

1. At his death the deceased was a tenant of the said premises under a written lease made in pursuance of *The Short Forms of Leases Act* of the Province of Ontario, which provided for a monthly rental of \$300 per month and the term of which did not expire until January 31, 1965.
2. The said lease constituted property passing on the death of the deceased.
3. The economic rental for the demised premises at the date of death of the deceased was \$200 per month.
4. The executor of the estate of the deceased would, at the date of death of the deceased, have been obliged to pay in the market to a substantial person in order to induce him to take an assignment of the lease (including an assumption of the obligations thereunder) the sum of \$3,460.
5. The value, at the date of death of the deceased, of the remainder of the term of the lease was, in the absence of any obligation to pay rent, \$4,340.
6. At the date of death of the deceased all rent which had accrued due under the lease up to November 30, 1962 had been paid by the deceased.

The Appellant submits that this leasehold interest has no "value" within the meaning of s. 58(1)(s)(ii) of the *Estate Tax Act* and therefore was not "property" as defined in s. 58(1)(o) of the Act and should not be included in computing aggregate net value of property passing on the death of this deceased under s. 3 of the Act, because there was no "fair market value" of this leasehold interest in that "the economic rental for the demised premises at the date of the death of the deceased was \$200 per month and the cost of

collecting this economic rental of \$200 per month was the rent payable under the lease, namely \$300 per month".

At the same time, the Appellant submits that he should be entitled to deduct in computing such aggregate net value as a debt of the deceased the sum of \$7,800 being the rental payable of \$300 per month for the unexpired term of this lease.

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Counsel submits that the Respondent in making his final assessment:

- (a) added the sum of \$4,340 to the aggregate net value of the property passing on the death of the deceased being the value at the date of death of the deceased, of the remainder of the term of this lease, in the absence of any obligation to pay rent, pursuant to the provisions of s. 3 of the *Estate Tax Act*; and
- (b) deducted the sum of \$7,800 as a debt of the deceased, being the rental payable over the balance of the term remaining of this lease at \$300 pursuant to the provisions of s. 7 of the *Estate Tax Act*;

(note that the sum of \$4,340 is a capitalized figure, whereas the sum of \$7,800 is not, and therefore if this assessment is correct, the Appellant was given a slightly larger deduction than he is legally entitled to),

and that the Respondent could also have legally assessed this leasehold interest on a net value basis.

It is patent that such an item of property as a leasehold interest for a number of purposes may have (i) no market value, (ii) a plus value or (iii) a minus value. (See re: *City of Toronto and McPhedran*<sup>1</sup>; *City Parking Ltd. v. City of Toronto*<sup>2</sup>; Challies, *The Law of Expropriation*, page 158 et foll.; *In re Brand*<sup>3</sup>; *In re Will of Inglis*<sup>4</sup>.)

For the purpose of the *Estate Tax Act*, R.S.C. 1958 c. 29 as amended, a leasehold interest as an item of property has no market value when a tenant is paying pursuant to his lease contract the full rental that the property is worth (i.e. the economic rental or in other words the "fair market value" within the meaning of s. 58(1)(s)(ii) of the *Estate Tax Act*); when a tenant is paying less than the economic

<sup>1</sup> 54 O.L.R. 87, Middleton, J. A. at p 91.

<sup>2</sup> (1959) 19 D.L.R. (2d) 689 and [1961] S.C.R. 336.

<sup>3</sup> (1945) Northern Ireland Law Reports 1.

<sup>4</sup> (1890) 8 N.Z.L.R. 28.

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rental his leasehold interest as an item of property has a plus value; and when a tenant is paying more than the economic rental it has a minus value.

The subject lease in this case has a minus value as an item of property for estate tax purposes. It is the amount of the burden of this leasehold on this estate that has to be assessed and allowed to be deducted from the value of the deceased's estate before determining the balance on which the estate tax is payable.

This can be done in two ways, namely by doing it the way the Minister has done, as referred to above in these reasons, or by valuing it on a net basis, that is by calculating what the executor of this estate would have been obliged to pay in this market to a substantial person in order to induce him to take an assignment of this lease including an assumption of the obligations thereunder. Such a sum the parties agree in this case would be \$3,400.

By either method the same result is obtained.

The appeal is therefore dismissed with costs.