EASEMENTS AND THE FEE SIMPLE INTEREST

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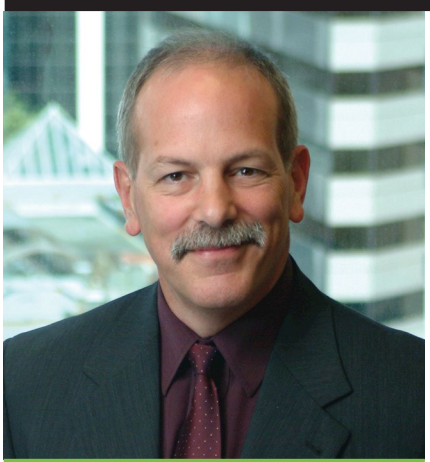

"IF ONE PURCHASES PROPERTY THAT HAS AN EASEMENT TAKEN BY EXERCISE OF A GOVERNMENT POWER SUCH AS EXPROPRIATION, THE BOARD'S VIEW OF THE DEFINITION OF FEE SIMPLE PERMITS THE EASEMENT TO BE TAKEN INTO ACCOUNT FOR ASSESSMENT PURPOSES."

How does an appraiser account for an easement registered against the fee simple interest in a parcel of land? Does it matter who is the grantee of the easement? Does it matter if the valuation exercise is for assessment purposes? These questions were recently considered by the British Columbia Property Assessment Appeal Board in *Five Mile Holdings Ltd.* v. Area 10 (2014 PAABBC 20140278) (*Five Mile*), where the issue was whether an easement registered against title to the subject property had to be considered in assessing the property.

The subject property was an apartment building and an adjacent parking lot structure. Some decades previous, an easement had been registered against the subject property granting a neighbouring property free and uninterrupted use of the parking lot structure. The easement was said to run with the land and could not be unilaterally removed by the owner of the subject property.

The owner of the subject parcel argued that the easement had to be taken into account (presumably with the result that the market value would be reduced). The Board did not agree.

By way of background, the *Assessment Act*, RSBC 1996, c 20, at section 19(1) defines "actual value" as "the market value of the fee simple interest in land and improvements." At paragraph 8 of *Five Mile*, the Board described the fee simple interest in terms mirroring those found in appraisal definitions for "fee simple":[1]

> ... broadest private property interest known in law. It encompasses absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the government powers of taxation, expropriation, police power and escheat.

The Board then relied upon the British Columbia Court of Appeal decision in *Standard Life Assurance Co. v. Assessor of Area #01 - Capital* (1997) CanLII 4012 [*Standard Life*].

Standard Life Assurance Co v. Area 01

In *Standard Life* the court rejected the owner's argument that contract rents in place at the date of valuation should be used to assess the owner's office tower, rather than the market or economic rents the assessor relied upon. In the course of rendering its decision, the court discussed the nature of the fee simple interest.

At paragraph 10 of *Standard Life*, the court recognized that the fee simple interest is the greatest estate and most extensive interest a person can possess. The court held that the fee simple interest includes all interests in real property – not just the owner's interest. In the context of *Standard Life*, this meant considering the landlord's interest and the tenant's interest. The court stated: "That, for practical purposes, leads to the conclusion that the totality of the interests properly considered should,

generally speaking, be the equivalent of the owner's unencumbered interest."

At paragraph 13, Hollinrake, J.A. writing for the court stated the following:

> As I have said, in my opinion, the "fee simple interest" is comprised of the entirety of the interests in the property. This bundle of interests includes both the tenant's and the landlord's interest. Implicit in this is the principle that consideration of actual rental value is, generally speaking, not relevant to the valuation of the "fee simple interest." This is because the actual rental value is relevant only to the owner's interest in the land and buildings, whereas the actual value in the [Assessment] ***Act*** is the totality of all interests in the land and buildings. The owner's interest and the tenant's interest, in principle, should reflect the market or actual value of the land and buildings. It is for this reason that I have concluded that the "fee simple interest" is, again generally speaking, the same as the owner's unencumbered interest.[2]

The Board in *Five Mile* seized on the phrase "unencumbered interest" in concluding that the easement registered against the subject property had to be disregarded. Further, at paragraph 9, the Board held that: ""Actual value," therefore, is the market value of the complete bundle of rights – not the market value of a bundle that is one stick short of a full load."

After discussing the nature of an easement (i.e., an interest in real property transferred to the owner of another property), the Board stated that an easement may or may not detract from the value of the property burdened by the easement. Nevertheless, in the Board's view, an easement registered against title results in an *encumbered* fee simple interest in property that, for assessment purposes, must be ignored. The Board buttressed its conclusion on the basis of its interpretation of the case law that, for assessment purposes, it is the market value of the totality of the interests in land that matters.

At paragraph 16, the Board wrote the following:

> [16] Even though an easement may run with the land and bind future purchasers, it is still an encumbrance to the fee simple. A subsequent purchaser purchases an encumbered bundle of rights. The price paid reflects the market value of the fee simple encumbered by the easement, or the market value of something less than the full bundle of rights which may or may not be different from the market value of the encumbered fee simple interest depending on the market. Unless that encumbrance arises from the actions of government, taxing, or expropriation authority, any impact on market value need not be considered for assessment purposes. Actual value for assessment purposes must reflect the market value of the unencumbered fee simple interest without regard to any effect on value due to the transfer of a partial interest.

In other words, if the Board decision is correct, even though the easement may reduce the amount for which the property can be sold, for assessment purposes the owner must be assessed as if the easement does not exist.

But, if the actual value of the property against which the easement is registered is not reduced to account for the burden of the easement, does this result in double assessing of the easement value? Is the land benefitting from the easement "positively encumbered" so that the value of the easement must be deducted. If not then the effect is to count the value of the easement twice – once by not deducting the negative value from value of the burdened property and once by not adjusting the benefitting property for the value of the positive encumbrance of the easement.

The owner of the burdened property will be paying taxes for the owner of the land benefitting from the easement unless, of course, the original grantor of the easement has had the foresight to make the grantee responsible for the assessment and taxation of the easement.

If the *Five Mile* decision is correct, another interesting consequence flows. If one purchases property that has an easement taken by exercise of a government power such as expropriation, the Board's view of the definition of fee simple permits the easement to be taken into account for assessment purposes, but if the easement was granted by a private individual at some time in the past, then the interest will be ignored because it falls outside the definition of unencumbered fee simple interest. This is a curious result indeed.

There is a good chance we have not heard the last of this issue, at least in assessment circles and perhaps in other fields.

End notes

1 *The Appraisal of Real Estate*, 3d Cdn. ed., The Appraisal Institute of Canada, at page 6.1: "The most complete form of ownership is the fee simple interest – i.e., absolute ownership unencumbered by any other interest or estate, subject only to the limitations imposed by the four powers of government: taxation, expropriation, police power, and escheat."

2 One can readily see how the court's approach works where, for example, a contract rent is below market. The landlord's negative interest in receiving below market rent is offset by the tenant's positive interest in paying less than market rent. However, can it work as well when the negative interest affects one property and the positive interest affects another property?

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