



MINISTRY OF AGRICULTURE, FOOD AND RURAL AFFAIRS

Lease Agreements Land Leases

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Introduction

Leasing and renting land are common practices in rural Ontario. The high capital cost of land makes leasing an attractive alternative to ownership. This Factsheet addresses the general issues to consider when entering into a leasing agreement. The terms renting and leasing are used interchangeably in this Factsheet.

Section 1. Lease Agreements

Human Components of a Successful Lease

Any form of business agreement requires a good deal of mutual respect and trust. Leasing land is no different. To be successful, the lease arrangement must satisfy both the landlord and the tenant. Before entering into a lease, the landlord and the tenant should consider more than just price. The compatibility of the landlord and the tenant and the fairness of the lease are important aspects to consider.

Checklist of a Successful Lease

Compatibility - Can you get along and discuss differences? ___yes ___no

Honesty - Do you trust the person you are dealing with? Have you had business dealings together before?
___yes ___no

Clarity - Are the obligations of each party clearly defined in the written lease? ___yes ___no

Equitable Terms - Do both parties agree to the terms of the lease? ___yes ___no

Flexibility - Can you adjust the lease if changes occur? ___yes ___no

Suitability - Does the lease fit the crop and encourage good agricultural practices? ___yes ___no

Advantages and Disadvantages of Leasing Land for Agricultural Use

There are advantages and disadvantages to all leasing arrangements.

Advantages

Lower Capital Investment

- Capital investment is shared between landlord and tenant.
- Landlord supplies land, buildings and perhaps some of the operating expenses.
- Tenant supplies labour, machinery and usually the major portion of the operating expenses.
- Operators can increase the size of their business with limited capital investment.
- Since leasing is an alternative to ownership, it is really a means of "financing" a land base.

Increasing Financial Efficiency

- When funds are limited, it is often more profitable to spend this money on seed, fertilizer, chemicals and machinery than on buying land.
- Investing scarce funds in land may severely restrict the money available for operating capital, thus lowering the efficiency of the farm business.

Obtaining Farm Experience

- Renting enables the beginning farmer to gain needed experience in the financial operation of a farm business before committing to a long-term investment in land.

- Renting enables an operator to learn more about land in an area and allows the flexibility to change farms or leave farming.
- Renting may enable an inexperienced farmer to obtain the managerial assistance or mentorship of a more experienced landlord.

Sharing Risk

- By renting, both the landlord and the tenant can share in the risks and profits of farming. This is particularly important to a farmer with limited capital. The extent of the risk-sharing depends upon the nature of the lease agreement.

Family Arrangements

- A family business arrangement might include a lease agreement whereby someone rents land from a parent or rents land from a third party and shares the machinery investment with the parent.

Providing Retirement Income

- A retiring farmer might consider leasing all or a portion of his or her land base rather than selling.
- Ownership of land provides a hedge against inflation.
- The income from the rent provides a form of "pension" income to live on during retirement.
- A farmer approaching retirement could gradually phase out of farming by renting a portion of his or her land and farming the rest of it.

Disadvantages

Lack of Security of Tenure

- Short-term leases create uncertainty for the tenant.
- Since machinery investment is matched to the land base, the cancellation of a lease could result in having machinery over capacity and a higher cost per acre.
- Short-term leases provide more flexibility for landlords since it is possible to change tenants quickly or to sell the land. However, short-term leases can work to the detriment of the landlord since they may not encourage sustainable farming practices by the tenant.

Lack of Efficiency, Conservation and Incentive to Make Improvements

- Short-term leases may discourage production efficiency. For example, some tenants may not use the optimum amount of fertilizer under a crop share lease unless the landlord shares in the expense of fertilizer.
- Most soil conservation practices are a long-term investment. Most tenants with a short-term lease are interested only in practices that will show results during the term of the lease.

People Problems

- As with any business venture involving two or more persons, disputes and disagreements can arise.

Availability of Credit

The tenant farmer usually has a more difficult time obtaining intermediate and long-term credit than does the owner-operator because:

- the lender may require land as security for the loan
- leased land does not build equity

- the lease is short-term

Lack of Bargaining Power and Managerial Control

- There may be situations where the landlord has greater bargaining power even though the tenant is a capable manager.
- The landlord may insist on making most of the management decisions even though his or her contributions to the lease may be substantially less than the tenant's. For example, the landlord may insist on certain crops being grown that the tenant feels are not the most profitable.

Lost Opportunity for Capital Gain

- Land prices have generally increased over time, although they do decline occasionally.
- Land appreciation is an added benefit to the landowner, even though the capital gain is not realized until the property is sold.

Potential Loss of Tax Deferral or Exemption

- Leasing land can in some cases prevent the use of both the tax-deferred transfer to children and the \$1,000,000 capital gains exemption.
- Consult an accountant.
- See [Section 2](#). Tax Implications of Land Leases.

Written Lease Agreement

The most important thing you can do as a tenant or landlord is to put your agreement in writing. This one action would eliminate the vast majority of disagreements that occur. Even though the handshake has been a long-standing method of doing business in the rural community and a verbal lease agreement is a valid contract, it has serious disadvantages. However, many farmers and landowners are reluctant to use a written lease for several reasons:

- Tenants and landowners alike do not want to give the impression that they distrust their neighbours by requiring a written lease.
- The added time and cost to prepare a written lease may not seem justified when dealing with other farmers or community members. The disadvantage of a verbal lease becomes apparent when a disagreement about the terms of the lease occurs, because it is exceedingly difficult to prove what the original understanding between the parties was.

Without a written agreement:

- Settling a misunderstanding between the parties once the land is in use (through mediation by a third party, arbitration or litigation) can be extremely costly.
- It is more difficult to protect the interests of both parties against any claims of a third or outside party to a right to the land or the crop. It is much easier to protect your interests from third-party claims by documenting the details of the agreement at the time you enter into it.
- The risk of losing significant time and business goodwill is high for both landowner and the lessee.

A written agreement is not a sign of distrust - it shows that both parties want to protect and clearly document the agreement they are making.

Advantages of a Written Lease Agreement

Under the Ontario *Statute of Frauds*, all documents that create an interest in land must be in writing. A written lease is advantageous to both the landlord and the tenant since it provides both with a record of what they have agreed to. If a dispute occurs, a written lease can prevent costly legal action by providing for alternatives

to a court proceeding. In the case of crop share leases, where the landlord and tenant are sharing costs, this is especially important. A written lease:

- clarifies the expectations, obligations and responsibilities of both parties gives the landlord some protection in the event of an environmental liability
- provides a valuable guide to heirs if the landlord or tenant should die
- provides documentation for tax purposes

What to Consider Before Entering Into a Lease Agreement

Insurance - Landowners may consider requesting proof of crop insurance, especially if the rent has not been prepaid. The tenant and landlord should also discuss insurance for protection from any potential environmental damage. If the tenant plans on storing any harvested crop on the landowner's property, there should also be insurance provisions for protection from theft or damage.

Securing the lease payment - Registering any unpaid portion of the lease payment with ServiceOntario under the Personal Property Security Registration will help protect a landowner's interest as a creditor in the event of non-payment by a tenant. Landowners may register online or by calling ServiceOntario.

A tenant may also want to have the lease registered against the title to be protected in the event that the land changes ownership. There may be very good reasons to consider the registration of the lease: for instance, any payments relating to the real estate can, in some instances, be considered "personal property" and fall within the registration provisions of the *Personal Property Security Act*; any interest in those payments would be subordinate to any other interest by way of a lease, so long as the lease is registered first.

Most properties in Ontario are registered under the Land Titles system, which dictates that leases for a period not exceeding three years do not require registration where the tenant is in actual possession of the property described in the lease. For properties under the less popular Land Registry system, the period is increased to seven years. In the absence of registration, a subsequent purchaser of the land could take ownership without having to honour the terms of the lease.

Title search - Tenants may also perform a search on the title of the land to be leased to make sure they are entering into an agreement with the person who is the owner of the land. A title search may be done through the Ontario Land Registry Office.

A Lease Agreement as a Succession Planning Tool

A long-term lease agreement (not to be confused with a sale and leaseback arrangement) may be used as a succession planning tool. Landowners and potential farm successors thinking about alternatives to traditional financing options might want to consider a long-term leasing arrangement. Lease arrangements may include land, buildings and/or equipment. Owners and successors may choose to have multiple lease arrangements or a single inclusive lease. Leases in Ontario can be of any length of maturity, however, leases longer than 21 years must have the approval of the municipality to be valid.

Like any lease, the terms must be negotiated to the satisfaction of both parties. One of the biggest difficulties after setting the initial lease payment amount is determining what the annual increase should be. For longer-term leases, an impartial setting, such as the annualized core Consumer Price Index, which is published by Statistics Canada, may be used. It is advisable to talk to a succession planning professional to help set out some of these terms.

Section 2. Tax Implications of Land Leases

The following is for general illustrative and information purposes only and is not comprehensive, nor is it intended to be legal advice. It does not replace professional advice from a tax specialist. Remember, tax laws and qualifications for programs may be time limited or may change. It is strongly recommended that you consult with a tax specialist for up-to-date advice that is specific to your agreement.

The tax implications of entering into a lease agreement should be carefully considered.

Landlords can inadvertently disqualify themselves from being able to use two major tax provisions. The Canada Revenue Agency (CRA) does not consider many types of leasing to be farming. For example, a share

crop lease, where a portion of the crop is given to the landowner as payment for the land, may not meet the CRA's definition of farming. As a result, some leasing arrangements can disqualify landowners from using the following tax provisions:

- the ability to use a tax-deferred rollover on the transfer of land to children (called a rollover)
- the \$1,000,000 capital gains exemption on their land

Tax Deferred Rollover to Children

The *Income Tax Act* allows for the transfer of farmland to a child on a tax-deferred basis. This is accomplished by using what is called a "rollover." It allows the transfer price to be set at any value between zero (a gift) and the fair market value (FMV) of the land. In the case of a gift, the transfer value would be the adjusted cost base (ACB). Without the use of the rollover, the land would have to transfer at its FMV and all the gain would have to be reported.

To qualify for the rollover, the property must have been used principally in the business of farming prior to the transfer by the taxpayer, the taxpayer's spouse or their children who were actively and continuously involved. This means that the land's use was farming for greater than 50% of the time (as defined by the CRA). The property does not, however, have to be used in farming immediately before a transfer takes place in order to qualify for the rollover.

Landowners who want to use the rollover should monitor the percentage of time that they have leased their land and what type of leasing arrangement they are using. For example, a landowner who farmed a property for 20 years, then leased the land for 4 years could still qualify for the rollover. If, however, the leasing period was longer than the farming period, it could disqualify the use of the rollover. An exception to this is if the person leasing the property is the landowner's spouse or child actively engaged in farming.

The \$1,000,000 Capital Gains Exemption

Selling Farmland

The \$1,000,000 capital gains exemption is available to individuals on the sale of qualified farm property. Individuals who had used their entire \$100,000 personal exemption, which was eliminated in 1994, have \$900,000 remaining. The exemption is also available for partners in a partnership, since taxes are paid at the individual level. However, corporations do not have any capital gains exemption.

Qualified farm property includes:

- farm land and buildings
- shares in a family farm corporation
- an interest in a family farm partnership
- quota (referred to as eligible capital property)

Qualified farm property must meet the following definitions:

- Property purchased before **June 18, 1987**, must be used in farming at the time of sale, or have been used in farming for any 5 years during its ownership.
- Property purchased after **June 17, 1987**, must be owned for 24 months prior to the sale, and in at least 2 years, the gross farm income must exceed net income from other sources or the property was used by a family farm partnership or corporation in a 2-year period during which time the individual, spouse, child or parent was actively involved in the farming business.

In either of the above cases, property must be used in farming by:

- the individual
- the spouse, child or parent of the individual, or
- a family farm partnership or corporation of the individual, spouse, child or parent

In all cases, the qualifying individuals, whether farming as a sole proprietorship, a partnership or as a shareholder in a farming corporation, must be actively engaged in management and/or the day-to-day activities of the business.

Leasing Farmland

Leasing farmland is most likely to affect the use of the exemption on land purchased before June 18, 1987.

Land purchased before June 18, 1987, must be farmed for **any 5 years or farmed in the year of sale** to be considered qualified farm property and therefore eligible for the capital gains exemption. If the 5-year rule has not been met, the property must be farmed immediately before the sale.

Since leasing is not considered to be farming, according to the Canada Revenue Agency (CRA), a lease in the year of sale could disqualify the landowner from using the capital gains exemption because it was not farmed immediately before the sale. Even a share crop lease, where a portion of the crop is given to the landowner as payment for the land, does not meet the definition.

Hiring custom operators to do the cropping work may solve this problem. Alternately, a share crop lease where the landowner is sharing the cost of inputs may also meet the CRA requirements of farming. Discuss such agreements with your accountant.

Canada Pension Plan and Registered Retirement Savings Plan

Rental income from a cash lease cannot be used as a basis for contributions to the Canada Pension Plan (CPP). Farmers who lease their land and have no other CPP-eligible income source will be unable to make contributions to the plan. This may have the effect of reducing the amount of CPP pension benefits. Although rental income is not eligible for contributions to the CPP, it is considered earned income for the purpose of contributions to a Registered Retirement Savings Plan (RRSP).

Rather than operating under a cash lease, a landowner could farm the property by hiring custom operators or lease the land on a crop share basis where the inputs are shared. Currently, the net income from these sources is eligible for contributions for both the CPP and RRSPs.

Non-Resident Withholding Tax

If the landlord is a non-resident of Canada, the tenant is required to withhold 25% of the rent (cash rental or crop share) and submit it to the Canada Revenue Agency (CRA). If the tenant does not remit the 25% withholding tax, the CRA will attempt to collect the tax from the landlord. If the landlord does not pay this tax, the tenant will be liable for the payment.

Capital Cost Allowance

When a landowner changes the use of the farmland, buildings or machinery, such as in renting, the *Income Tax Act* Regulations require that the depreciable assets purchased before 1972 (Part XVII) be switched from the Straight Line Method of capital cost allowance to the Declining Balance Method, which is used for depreciable assets purchased after 1971 (Part XI).

In most cases, this is undesirable, since it would mean that all recaptured capital cost allowance that occurs when the class is closed out (e.g., sale of all machinery in that class) would be taxable income. The landlord could choose to not use the property and still maintain the Part XVII status, however, no deduction could be claimed in the years when it was not used. Any other use, either personal or rental, would require a change to Part XI. The landlord could choose to use his machinery or buildings as part of a custom farming arrangement and thereby maintain the farming status.

Harmonized Sales Tax (Hst)

Generally speaking, a lease is taxable unless specifically exempted under Part I of Schedule V of the *Excise Tax Act*, which might apply in limited situations such as land destined as a long-term residence. Rent that is paid by way of share of the crop is not subject to the HST. The treatment of cash rents for HST purposes may also depend on the landlord's total income. A business (including a landlord who rents property) does not have to register to collect and remit HST if its gross taxable and zero-rated sales are under \$30,000. Landlords whose only source of business income is rent, where the rental income is less than \$30,000, need not register, although they may choose to do so.

Farm Property Class Tax Rate Program

The Farm Property Class Tax Rate program enables eligible farm properties to be taxed at 25% of the municipal residential/farm tax rate. The farm residence and 1 acre of land surrounding it are taxed as part of the residential class.

To be eligible for the reduced rate, an application to the program must be filed showing that the property is used by a farming business with a valid Farm Business Registration number that has gross farm income of \$7,000 or more. Exceptions to this threshold can be made for new farming operations. For more information, contact the ministry, toll-free, at 1-877-424-1300 or visit the website at www.ontario.ca/farntax <<http://www.ontario.ca/farntax>>.

Section 3. Elements of a Lease Agreement

The Components of a Lease Agreement

A written lease can be as simple or detailed as the landlord and the tenant wish. The following summary presents the items that a lease can contain, categorized under three headings.

Items in Written Lease Agreements

Required Items

- names and addresses of tenant and landlord
- description of property to be rented
- term and renewal of the lease
- rent payable, payment and use of utilities

Recommended Items

- right of inspection and removal of crops
- transfer of property
- termination of the lease
- use of the land
- environmental matters
- insurance
- rights to assign or sublet the lease
- resolution of differences
- restrictions of land use

Optional Items

- production practices and management decisions
- income support payments, subsidies and reimbursements
- repairs to buildings, fences and improvements
- duty to notify Agricorp
- compensation for property damages
- rights of first refusal
- option to purchase
- miscellaneous
- municipal zoning restrictions

Required items

All leases must contain this information:

Names and addresses of the tenant and landlord - Including spouses if required.

Description of property to be rented - Includes the legal description and specifies buildings or areas to be excluded.

Term of the lease - Indicates when it starts and how long it lasts. Although not a basic requirement of a lease, this section should also address the renewal of the lease if the parties wish to maintain the lease agreement for a period of years, including when and how such a renewal will take place.

Rent payable - The amount of rent, how it is calculated and when it is to be paid. In the case of a building lease or where the renter has access to facilities, the payment and use of utilities should also be stipulated.

Recommended Items

Items that every landlord and tenant should consider including in the lease agreement:

Right of inspection and removal of crops - Includes the following:

- The landlord should have the right at all times to inspect the rented property.
- The tenant should be able to complete harvesting of the crop after a reasonable time period after the termination of the lease agreement or the sale of the property. If this is not possible, the landlord will compensate the tenant for the anticipated agreed upon value of the crop.
- The incoming tenant, purchaser or landlord should have the right to enter on the land after harvest in the last year of the agreement to prepare the land for next year's crop.

Transfer of property - It is important that the landlord and tenant discuss their expectations in the event that the landlord sells the farm property to a new owner during the term of the lease. A fair agreement will attempt to strike a balance between the landlord's desire to not unduly restrict his or her ability to sell the farm and the tenant's desire to continue the lease arrangement.

Termination of the lease - The lease should clearly spell out how it can be terminated. This could be due to a breach of the terms of the lease or merely because the termination date of the lease has arrived.

Use of the land - The lease should state how the tenant is going to use the land. The lease should also describe any certification, regulatory or contractual constraints that the renter should be aware of, such as the land being certified as organic. The tenant should be required to adhere to normal farming practices in regard to disposal of manure. It should also be clearly stated how the land is to be left after termination of the lease. If buildings are included in the leased property, the lease should state how the buildings will be used and the rules for accessing the buildings.

If the farm will be used for selling products such as pick your own fruit, the lease should indicate this, and the tenant should be made aware of all the regulations governing the sale of food products, in addition to food safety requirements.

Environmental matters - This clause addresses the issue of environmental policies and responsibilities. In the event of an environmental problem, landlords, as owners of the lands, are ultimately responsible for activities occurring on their land. The tenant, as "user" of the land, should agree to adhere to appropriate and accepted farm practices and legislation relating to the environment (manure disposal, pesticide and herbicide applications, etc.). The tenant should also provide a "warranty" - a legal term meaning that this assurance can be legally relied upon - that they possess the necessary provincial licences for the application of pesticides or other chemicals to be used on the property.

Normally the tenant bears the cost, including the costs associated with an environmental clean-up, and reimburses the landlord for any costs that the landlord incurs as a result of the breach by the tenant of any environmental regulation.

Insurance - A clause regarding insurance would allow the landlord and tenant to identify who will be responsible for insurance coverage. The parties should ensure that adequate policies of insurance coverage, including occupier's liability insurance (insurance against personal injuries sustained by people coming onto the farm property) and fire insurance (especially if buildings are included), are in place.

Rights to assign or sublet the lease - The written agreement should contain a clause that prevents the tenant from subletting or assigning the lease to another individual without the written consent of the landlord. In a production lease, the consent of the landlord can be withheld at the landlord's sole discretion, without explanation or reasonable cause (i.e., unreasonably withholding consent). In the case of a residence, the landlord cannot unreasonably withhold consent.

Resolution of differences - An arbitration or mediation clause in the written agreement describes how to deal with disagreements the tenant and landlord cannot resolve. The most common practice is to appoint a mutually agreed upon third party to act as a mediator or arbitrator.

Restrictions of land use - The lease should clearly define any areas that may have restricted use (e.g., the area directly underneath a wind turbine).

Optional Items

These items add clarity to the lease agreement and provide discussion points for the landlord and tenant as they formulate the lease agreement:

Production practices and management decisions - This clause deals with production and management decisions the landlord wants carried out by the tenant. Some of those factors could include:

- cropping decisions
- proper use of fertilizer and chemicals
- crop insurance and revenue insurance
- delivery and sale of crop

Income support payments, subsidies, reimbursements - The written agreement should clearly specify how government or marketing agency payments will be divided. This is most relevant in a crop share lease.

Repairs to buildings, fences and improvements - A clause stating who is responsible for repairing buildings, fences and other improvements, and how the expenses will be shared. A common practice is to have the tenant responsible for all minor repairs and for the landlord to reimburse the tenant for improvement costs that have a lasting benefit longer than the rental term.

Examples of major improvements that extend beyond the length or termination of the lease are:

- building and fence construction
- erosion control
- tile drainage
- clearing land

It is usually required that tenants obtain written permission from the landlord before making major improvements. It is also important to outline how the value of improvements will be determined and when compensation will be made. An example of one form of compensation to the tenant for improvements is for the landlord to let the tenant farm the improved land rent-free for a specific period of time to be agreed upon between the parties (in writing) at the time the improvement is consented to by the landowner. An annual review and agreement of the repairs and improvements needed could also be included here.

Duty to notify Agricornp - Both the landlord and tenant must notify Agricornp of any crop-sharing arrangement.

Compensation for property damages - This clause is especially necessary for determining responsibility for third-party and environmental damages.

Right of first refusal - In some cases, the tenant is interested in purchasing the leased land but is either unwilling or unable to do so at the time. In these cases, the landlord may be willing to include an option whereby the landowner will notify the tenant that there is an offer to purchase from another party, allowing the tenant to bid on the purchase of the land before the landowner accepts the offer to purchase the land from the other party.

Option to purchase - The parties may include an option similar to the right of first refusal that allows the tenant to purchase the leased lands. This could be for a limited or unlimited time and for either a fixed price or a price to be determined by some objective method such as a real estate appraisal by a certified agricultural appraiser.

Miscellaneous - The lease agreement may contain a clause that would terminate the lease if certain natural disasters occurred. For example, if the land were flooded and the tenant were unable to use the property, it would be unfair to insist the tenant continue to pay the cash rental unless the original rent charged had considered the risk of flooding. Other unforeseen circumstances include the installation of a highway, gas line, oil well sites, etc., on the rented land, creating inconvenience and additional operating costs for the tenant. In some instances, instead of terminating the lease, it may be considered desirable to renegotiate the terms of the lease or compensate the tenant for the added costs or reduced income they may incur.

Municipal zoning restrictions - The tenant enters into a farm lease with the express intention of conducting agricultural operations; it is important that the landlord provide an assurance to the tenant that the lands are properly zoned for such use. If the landlord is unwilling to provide such a warranty, the tenant should get advice from the local municipal authorities to ensure that the purpose to which the tenant wishes to put the property is permitted.

Section 4. Termination and Other Legal Issues

Termination of the Farm Lease

A farm lease can be terminated in a number of different situations, including:

- **Termination at the end of the specified term in the lease.** If a tenant remains in possession of the property after the termination date without the consent of the landlord, then the landlord can obtain a court order to have the tenant removed.
- **The surrender of the lease by the tenant.** That is, the voluntary "giving up" of the lease with the consent of the landlord.
- **The merger of the lease.** The tenant purchases the leased property from the landlord.
- **The foreclosure of the lease,** in the event the landlord defaults on any mortgage on the lands, and the mortgagee begins foreclosure proceedings. This would normally only apply if the lease was entered into after the registration of the mortgage in the land registry office.
- **The giving of notice by the landlord to the tenant of the intention to terminate the lease.** If the lease does not expressly state a termination date, then the landlord is required to give notice in accordance with the *Commercial Tenancies Act* (Ontario). Weekly tenants must receive 1 week's notice; monthly tenants receive 1 month's notice [Act, s. 28]. The legislation appears to be silent on the amount of notice required for a yearly lease, so it is critical the parties set out the appropriate length of notice in the written lease.

Tenant's "Relief from Forfeiture"

The tenant has certain rights in the event of termination of the lease by the actions of the landlord.

In legal terms, the tenant benefits from the principle known as "relief from forfeiture." This means that where a landlord is proceeding to terminate the lease, whether for non-payment of rent or other cause, the tenant may apply to the courts to remain in possession of the premises upon such terms as the courts direct, if the termination of the lease would result in significant harm to the tenant's enterprise. It is up to the tenant to make a substantial case for relief from forfeiture in the event that the tenant has otherwise breached the terms of the lease.

Non-Payment of Rent

The *Commercial Tenancies Act 1990* c L7 (Ontario) contains some specific issues relating to farm leases. Most of these provisions relate to the options available to a landlord when a tenant fails to pay rent. The Act permits the landlord to seize the goods of the tenant for the purpose of selling those goods in payment of the rent due to the landlord. This is called the remedy of distress.

Section 45 of the Act allows a landlord to seize and secure goods if rent is unpaid and to sell the goods if the rent remains unpaid. "Goods" includes the tenant's livestock and growing crops. The landlord can seize and harvest ripened standing crops for arrears of rent and place them in an appropriate facility until the rent is paid or they can be sold. In this case, the tenant is granted the right to know where the crop has been taken. In the event the tenant then pays the rental arrears, together with any costs incurred by the landlord in pursuing this remedy, the tenant is entitled to receive the crops back.

Section 46 of the Act specifically exempts sheep and animals used in ploughing and preparing the lands for crops from the distress remedy if there are other chattels sufficient to pay the amount owing.

Note that in the case of an insolvent tenant, other creditors might have priority security agreements that rank prior to the interests of the landlord (especially if the landlord has failed to register or secure his interest and is therefore an unsecured creditor).

However, it has been established that fixtures that can be severed from the real property and restored to their character as chattels are not distrainable at common law ("distrainable" is a legal term meaning to be held in custody in order to satisfy an unpaid debt). (Source: *859587 Ontario Ltd. v Starmark Property Management Ltd.*, Ontario Court of Appeal, 1998.)

Registration of the Lease

Generally, a lease with a long duration (e.g., land leases through the Feed-in Tariff contract) will be registered. This is done through the Land Registry Office. The registration of the lease against the property title provides notice to potential buyers or mortgaging agents of the tenant's interests in the land.

Spousal Obligations

Farm leases are unique in that the farmland is generally used for dual purposes. One use is for business activities, while the other is for the family residence of the owners. The *Family Law Act* (Ontario) provides, among other things, that one spouse cannot create an interest in land, including a leasehold interest, without the consent of the other spouse if the interest impacts on the use and enjoyment of the "family residence" or the land is jointly held. As such, if the farm lease is to include the personal residence located on the farm property, it is important that both spouses acknowledge their consent to the lease.

Assignment and Subletting

Section 23 of the Commercial Tenancies Act stipulates that, unless a lease provides to the contrary, assignments or subletting to a third party can occur with the consent of the landlord and that such consent cannot be arbitrarily withheld by the landlord. This requires the landlord to consent to any reasonable new party taking over the terms of the lease. Because of this legislation, farm leases often contain a clause that permits the landlord to arbitrarily not consent to such an assignment.

The Landlord And Tenant Relationship

The relationship of landlord/tenant can sometimes be confused with the relationship of joint venture or partnership. Because the legal obligations of these relationships are very different, it is important to clarify the relationship that is intended in a lease agreement. This is especially true in the case of a crop share lease where both parties are contributing to a cropping enterprise. The lease should clearly identify the parties as having the relationship of landlord and tenant, if that is the intent of the business relationship.

The Farm Employee Tenant

The *Residential Tenancies Act, 2006* (RTA), deals primarily with the use of residential units in Ontario. However, the provisions of that legislation specifically exempt living accommodations of farm employees. This means that the specific rules regarding residences in the legislation do not apply to farm workers who benefit from the use of farm residential premises as a term of their employment, whether or not the residential premises are located on farm property.

Section 5. Types of Leases

There are several types of cropland leases, including cash rental, flexible cash rental and crop share rental leases. What makes each of these leases different is how the payment for the land is calculated. Cash rental is fixed. Flexible cash rental and crop share rental are based on a division of revenue from the crop in a pre-determined fashion. In addition to cropland leases, there are building and pasture leases.

Cropland Lease Comparison

Cash Rental Lease

- Tenant receives the income from all crop sales but pays the landlord a fixed dollar amount each year as the rent.
- A portion of the rent may be paid in advance and the rest at harvest.
- The tenant bears all the production risk.

Crop Share Lease

- Crop sales are divided between the landlord and the tenant.
- Income is divided as the crop is sold.

Flexible Cash Rent Lease

- Tenant receives all the income from crop sales, but the dollar amount paid to the landlord each year varies with either the price of grain or yield of grain, or both price and yield.
- This type of lease incorporates features of both the Crop Share and Cash Rent leases.

The amount of risk borne by the tenant and landlord depends on the type of leasing arrangement. Generally a cash rental lease arrangement would, over time, return less to the landlord than a crop share arrangement. In a cash rental lease, the landlord does not share any of the risk or benefits associated with growing the crop or crop yield variation and therefore does not reap the returns when prices or production are higher than normal.

The risks associated with the various leases can be grouped into two categories, namely production and marketing risk. [Table 1](#) outlines these risks and shows which risks are shared by the landlord under the three types of lease arrangements discussed.

Table 1. Comparison of Landlord's Risk Under Three Types of Lease

Type of Risk to Landlord's Income	Type of Rental Lease		
	Cash Rental	Crop Share	Flexible Cash
Production <ul style="list-style-type: none"> • weather • insects and disease • use of inputs • general management 	No	Yes	Yes
Marketing <ul style="list-style-type: none"> • price variations • crops grown • delivery opportunities • storage costs and losses 	No	Yes	Yes

Establishing a Rental Rate

Most rental rates are established by using local market rates, which reflect the supply of and demand for rental land in a local area. Crop share and flexible cash agreements use this market rate as the basis for establishing the crop shares or flexing provisions in the agreement.

Despite the fact that most rental agreements are based on local market rates, a tenant and landlord should take the necessary time to calculate their costs and potential revenues from their proposed arrangement. This

will help them determine if the arrangement will be profitable. Calculating and knowing the potential costs and revenues is also useful when good market comparison data is not available.

It is important to emphasize that determining a fair cash rental rate or crop share depends on the landlord and tenant knowing their costs. In addition, estimates for labour, depreciation, management and investment must be taken into account.

Several approaches can be used to determine an appropriate rental rate. These methods are summarized in [Table 2](#). These calculations give you a place to begin your negotiations and, more importantly, provide a safeguard against entering into agreements that are unlikely to be profitable.

Table 2. Methods of Calculating a Rental Rate

Method	How It Is Calculated	Pros	Cons
Current market approach	<ul style="list-style-type: none"> The going rental rate and conditions in the area establish the rent for the land. Both parties should do their own financial projections to determine if returns will be adequate to make the leasing worthwhile. 	<ul style="list-style-type: none"> This method is usually used above all others 	<ul style="list-style-type: none"> This is difficult to calculate if local rates can't be determined. There can be a large variation even within a small geographic area due to type or condition or competition for land.
Landlord's cost approach	<ul style="list-style-type: none"> Landlords determine how much cash rental is necessary to give the desired rate of return on land investment. 	<ul style="list-style-type: none"> This method can be used as a start-ing point for land-lords. 	<ul style="list-style-type: none"> The amount is often higher than the going market rate because the landlord's capital gain is not included.
Crop share equivalent approach	<ul style="list-style-type: none"> This method is used to establish or negotiate a cash rental rate. Landlord estimates amount of rent received based on a normal crop share lease. 	<ul style="list-style-type: none"> Both landlord and tenant can see how the cash rent figure is calculated. This method is useful as a starting point. 	<ul style="list-style-type: none"> This requires knowing the costs involved. This method may be more difficult for the inexperienced. This requires knowing the normal crop share arrangement.
Income approach	<ul style="list-style-type: none"> Income and expenses for a given situation are estimated and net income is calculated. Tenant or landlord set rent based on a return to labour or investment. Tenants use this 	<ul style="list-style-type: none"> Tenant and landlord can calculate their own costs and revenue. 	<ul style="list-style-type: none"> Because income and expenses are estimates, inexperienced landlords or tenants may find this difficult to calculate. This method may not be appropriate for

	approach to determine how much rent they can afford to pay.		new crops or land rented for first time.
Contribution approach	<ul style="list-style-type: none"> Parties share the income from the land in the same proportion as they contribute to costs. Tenants receive a larger share if they contribute more in the way of crop inputs, machinery, labour or if they accept a larger risk. Landlords receive a larger rent for more productive and higher-valued land. 	<ul style="list-style-type: none"> This method recognizes the risk and investment of both landlord and tenant. 	<ul style="list-style-type: none"> It can be difficult to determine or agree on costs and value of investment, or the return required on the investment. Landlord may not be familiar with crop costs.

Sources of Cost Information

From [Table 2](#) you can see how important it is to know your costs when negotiating a rental rate. Your own records are the best source of this information, however, when these are not available it is important to use realistic estimates. Publication 60, Field Crop Budgets, is updated annually and available at ontario.ca/agbusiness. The 12 crop budgets provide you with cost estimates for comparison purposes.

Summary

Leasing land will continue to be an important method of controlling land without having the capital costs of ownership. Developing clear leasing arrangements is a benefit to both the landlord and the tenant.

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