

1-Minute Read for Commercial Mortgage Lenders: Beneficial Ownership vs. Registered

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Ownership of real property in Ontario is divided into legal or registered title ownership and beneficial ownership. Legal ownership and beneficial ownership of real property is often held in the same entity, however, in many cases, they are held in different entities. Lenders must take certain steps to properly secure their interest in real property where there is separation of legal and beneficial ownership. Simple inquiry into the ownership structure behind the underlying real estate asset can have a large impact on a loan transaction.

A common type of separation between legal and beneficial ownership is effected using a nominee relationship. This exists where there is an asset that is held by a bare trustee or nominee for the benefit of a third party beneficiary or beneficiaries. Beneficial owners may wish to establish a nominee to hold assets where, for example, the beneficiaries do not wish to be disclosed; to facilitate logistics of execution of contracts; or where the beneficiaries are not legal entities capable of holding title to real property.

Under a nominee arrangement, the beneficial owner appoints a bare trustee or nominee to act as agent and, generally, has no discretion to deal with the asset other than upon the direction of the beneficial owner. Given that the beneficial owner retains authority to deal with the asset and the nominee or bare trustee acts only upon the direction of the beneficial owner, it is ultimately the beneficial owner who is liable for the debts and obligations incurred by the nominee or bare trustee.

Case law has upheld the principle that allows an undisclosed principal to be shielded from liability where a bare trustee or nominee enters into a contract under seal, such as a mortgage of real property. **Where an asset is held in trust by a nominee or bare trustee for third party beneficiaries, it is essential that a beneficial owner's agreement be included as part of the security package.** A beneficial owner's agreement from the nominee and beneficiary is an off title agreement to charge the beneficial owner's interest in the subject property.

Where there is a separation of legal title and beneficial ownership, the following should be closely considered by a commercial lender when securing its interest in the underlying real property asset:

- Ensure a well-drafted beneficial owner's agreement is in place that: confirms the relationship between the nominee and the beneficial owner, authorizes the nominee to enter the mortgage, confirms the beneficial interest in the property is subordinate or postponed to the mortgage and other security and confirms that there are no existing liens on the beneficial owner's interest in the property, and restricts transfer of beneficial interest.
- Attached to the beneficial owner's agreement should be the nominee or bare trustee agreement which confirms the terms upon which the property is held and who the beneficiaries are and what threshold of beneficiaries is required to authorize action by the nominee.
- The lender should ensure appropriate authorizing resolutions are obtained to ensure the authorization of all parties to enter into the transaction.
- To the extent there is any personal property security related to the real property asset (i.e. PPSA registrations), the lender will want to register under the PPSA against not only the nominee but also the beneficial owners.
- The lender should require the beneficial owner to covenant that there will be no change in the beneficial ownership of the property without the prior written consent of the lender.

- The beneficial owner should confirm that the lender is entitled to deal with the security and the nominee without notice to the beneficial owner. However, a lender would not necessarily want to rely upon this clause where there are significant changes to the obligations or security or in taking steps to enforce against the property.
- The lender should require the beneficial owner to covenant to execute such further documents and provide any other deliveries required by the lender, including regular financial statements.

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