REAL PROPERTY

‘Are we closed yet?’ Some tools to solve new challenges

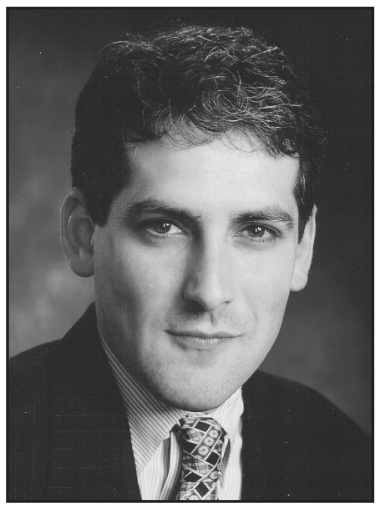
By Ira Barkin

Are we closed yet?” This question is posed with more impatience to real estate lawyers than it is to our colleagues practising law in other areas. Such is life when the time of closing is dependent less upon the resolution of outstanding issues than upon the speed with which registration numbers are issued by government bureaucracies.

As real estate transactions increasingly move into the area of capital markets, the question “are we closed yet?” raises new challenges.

When units of Real Estate Investment Trusts (REITs) or shares of other publicly traded entities (of which real estate assets comprise a material part) commence trading, the public relies on the issuer’s title disclosure. Since most units or shares commence trading at the opening of the stock exchange on which they are traded (typically 9:30 a.m. ET when the Toronto Stock Exchange opens), title to the real estate must be confirmed prior to this deadline.

Of course, this presents a problem when it is not possible to confirm title before 9:30 a.m. ET on the day of closing. Even when it is possible, the experience of most real estate lawyers tells us that there is no certainty when it comes to the timing of registering real estate documents. Absent such certainty, title is better dealt with prior to the day of closing than on the day of closing.



Ira Barkin

Pre-closing title confirmation may also prove to be an effective solution to the Canadian Payments Association’s Large Value Transfer System (LVTS) which provides that all payments for sums in excess of $25 million (Cdn) must be made by electronic transfer. LVTS came into effect on February 3. As if the pressure surrounding a 9:30 a.m. ET closing were not enough, we must now contend with the frustrating world of mandatory wire transfers.

If the solution to the problem is to confirm title prior to the day of closing, the question becomes how to best effect pre-closing title confirmation. In many transactions, commercial title insurance may prove to be the best solution. If requested, commercial title insurers will provide a “gap” endorsement insuring over the liability associated with the possibility of intervening registrations between the period commencing at the time closing proceeds are released and ending at the time title is transferred.

However, while the use of commercial title insurance policies has increased significantly over the last few years, a surprising number of business entities resist purchasing title insurance. This resistance is often understandable because it often stems from what many clients see as a redundant cost given that commercial title insurance companies require a title opinion prior to issuing a commercial title insurance policy. Where a title opinion already exists, there is less resistance.

‘[I]t continues to amaze me how many significant parcels of real property have been transferred over the years without any form of title opinion being delivered.’

However, it continues to amaze me how many significant parcels of real property have been transferred over the years without any form of title opinion being delivered.

Where title insurance is not an option, pre-closing title transfer tools need to be explored. For example, one could simply register a deed in favour of the purchaser in advance of closing. At the same time, the vendor’s solicitors would hold a deed, in escrow, conveying the real property back to the vendor, which deed would be released from escrow and returned to the purchaser upon closing. If closing does not occur within the time set out in the escrow arrangement between the parties, the deed in favour of the vendor would then be registered.

One obvious disadvantage arising from this solution is the potential double payment of land transfer tax.

Additionally, it is likely that any lender that holds security against the real property would have consent rights.

Moreover, because the vendor may not exercise absolute control over the purchaser, it is possible that the purchaser could register an encumbrance against title to the real property, so that the registration of the transfer back to the vendor will not result in the vendor acquiring title in the same state in which it was originally conveyed to the purchaser.

see CLOSING *p.14*

Real estate developer does not require realtor’s licence

By Heather J. Innes
Edmonton

The Alberta Court of Queen’s Bench has ruled that the usual activities of a real estate developer are not activities for which it needs a realtor’s licence, and the unpaid performance of such activities does not warrant the filing of a builders’ lien.

The parties’ principals met in 1988 when ESA Holdings Ltd. owned raw lands adjacent to those of Marquis Scenic Acres Development Inc. in Calgary. Marquis employed Ronald Slater, principal of Caleron Properties Ltd., at the time to handle the residential development of the adjacent lands.

ESA and Caleron agreed, by letter of intent, that Caleron would be responsible for management services and marketing of the ESA lands. The letter contemplated a management fee for Caleron based on a percentage of gross development costs and gross sales.

Caleron drafted development management and marketing agreements which were sent to ESA, which signed some of the drafts and gave them to its lawyer to hold in trust. Caleron did not know which, if any, of the drafts had been signed.

Slater and Caleron, through a numbered company, later negotiated purchase of other lands adjacent to the ESA lands, which were developed and sold between 1993 and 1995.

Ongoing problems regarding ESA’s payment of Caleron’s accounts led to Caleron filing a builders’ lien for its project management and consulting engineering services in December 1994. It also filed caveats on 14 individual lots in March 1995, pursuant to the unexecuted development marketing and management agreements.

When Caleron sued ESA for breach of contract, ESA counsel Tom Mayson of Fraser Milner Casgrain LLP, contended that under the *Real Estate Agents Licensing Act*, Caleron was not entitled to be reimbursed for its development work, as it did not hold a realtor’s licence, and that Caleron was in a conflict of interest due to having an undisclosed interest in the adjacent properties.

ESA also brought a statutory counterclaim against Caleron, alleging damages as a result of the wrongfully filed builders’ lien and caveats.

Justice Rosemary Nation rejected allegations that Caleron was acting as an unlicensed realtor and had an undisclosed interest in adjacent lands.

Reviewing the definition of “trade” in the *Real Estate Agents Licensing Act* and considering whether Caleron’s development management activities were “in connection with a trade in real estate as defined in the Act,” Justice Nation said that the development management activities did not meet the definition of “trade.”

With respect to the marketing commission claimed, Jeff Moroz of Calgary’s Shea Nerland Calnan argued on behalf of Caleron that the client’s marketing activities did not fit within the scope of the Act, either.

The judge said that while a broad reading of “trade” could include some Caleron activities, “when I consider the reason for the Act, the nature of the services provided by Caleron (supervising engineering, landscaping, signage) and the fact that Caleron did not deal with ultimate purchasers, had no involvement in the negotiation of the sales, and only was a conduit for already completed legal papers to counsel, I do not find that its activities fall under the definition in the Act, which would require it to be licensed to maintain an action.”

see CALERON *p.14*

Ontario Superior Court certifies real estate agents’ class action

By John Jaffey
Toronto

An Ontario Superior Court judge has certified a class proceeding against Ottawa’s Re/Max Metro-City Realty Ltd. (Re/Max) on behalf of past and present salespeople who allegedly overpaid the firm for their errors and omissions insurance premiums.

Clause 7 of the standard-form Re/Max contract with its salespersons requires them to pay “the amount the corporation determines in its discretion to be fairly attributable for any errors and omissions insurance from time to time maintained by the corporation for the benefit of its salespeople.”

Two former salespeople, Dianne Wilson and Michel Rousseau, commenced an action claiming a refund with interest for all amounts in excess of actual premiums paid to the insurer for insurance coverage. They also sought punitive damages on grounds the conduct was intentional and wrongful.

Wilson and Rousseau submitted that Re/Max had breached the standard contract and violated its fiduciary duty to each salesperson. They relied on the 1999 unreported decision of a wrongful dismissal case — *Doug Job v. Re/Max Metro-City Realty Ltd.* — which interpreted Clause 7 to mean that Re/Max could charge only “the amount fairly attributable to the premium … and any amount collected by Re/Max in excess of such premium in any year was improperly collected.”

Re/Max’s position was that all amounts collected were within the scope of the agreement and industry norms. It did not deny that it had charged more than the actual premiums. It also submitted that some of the class members would be barred by the *Limitations Act*.

In seeking certification as a class proceeding, Wilson and Rousseau also asked that they be named as representative plaintiffs.

Justice Michel Charbonneau reviewed each element of a five-part test in s. 5(1) of Ontario’s *Class Proceeding Act*.

Noting that Re/Max had conceded that the pleadings disclosed a cause of action, he disagreed with an assertion by the defendants that the plaintiffs had failed to demonstrate an identifiable class.

see RE/MAX *p.14*

REAL PROPERTY

Many vendors not comfortable at relinquishing control over title

CLOSING

–continued from page 9–

While this last obstacle may be overcome by the registration of a caution or similar instrument that prevents the transferee from registering encumbrances, many vendors will simply not be comfortable in relinquishing any measure of control over title to their real property until closing.

Another method of accomplishing registration in advance of closing involves the granting of a beneficial transfer. These transactions often involve the following steps:

(a) prior to closing (leaving enough time for the applicable registry office to provide confirmation of registration),
  (i) incorporate a company to act as a bare title nominee for and on behalf of the vendor (preferably the nominee company should have no history and, therefore, no assets or liabilities);
  (ii) deliver a nominee agreement whereby the nominee corporation agrees to act as nominee for the vendor, as beneficial owner;
  (iii) transfer title from the vendor to the nominee corporation for nominal consideration; and
(b) on closing,
  (i) transfer beneficial title from the vendor to the purchaser for full consideration;
  (ii) deliver an amended and restated nominee agreement whereby the vendor, the nominee corporation and the purchaser agree that the nominee corporation now acts as nominee for the purchaser, as beneficial owner; and
  (iii) transfer the shares of the nominee corporation from the vendor to the purchaser.

The advantages of taking these steps, as opposed to simply transferring title to the purchaser with an escrow transfer back to the vendor, are at least threefold.

First, with respect to land transfer tax, there may be a considerable savings, since title is transferred for nominal consideration.

In Ontario, this should avoid the possibility of the double payment of land transfer tax, since land transfer tax would only be paid within 30 days following closing of the beneficial transfer. If closing does not occur, the vendor would simply retain control over the real property through its nominee.

Second, with respect to lender approval, many loan documents allow the borrower to transfer real property without the consent of the lender if the transferee is an affiliate of the borrower. Third, with respect to control issues, since the nominee corporation remains a subsidiary of the vendor until closing, the vendor retains full control.

Structuring a transaction using beneficial transfers is not without potential problems. With respect to land transfer tax, careful consideration should be given to any previous dealings with the nominal and beneficial ownership of the property by the vendor, as there may be negative land transfer tax consequences depending on such previous dealings.

In other provinces, registration/land transfer tax is paid on the actual value of the property as opposed to the consideration, such that the potential double payment of land transfer tax may not be avoided. In other provinces, the rate of land transfer tax may be sufficiently low such that the potential double payment of land transfer tax is not a practical concern.

With respect to lender approval, some loan documents may contain consent rights in favour of the lender notwithstanding that the transfer is to an affiliate of the borrower. With respect to control issues, since the vendor has control over the nominee corporation prior to closing, the purchaser will be inheriting a nominee corporation whose history, however brief, cannot be known by the purchaser with absolute certainty. Accordingly, the purchaser will be taking on an unknown liability. If this is a practical concern to the purchaser, the purchaser should seek an appropriate indemnity from the vendor.

Whether it be through title insurance, escrow transfers or beneficial transfers, there are tools available to real estate lawyers which, if used appropriately, allow us to effectively deal with some of the significant time pressures placed upon us.

Ira Barkin is a partner with Goodmans LLP practising in the firm's Commercial Real Estate Department.

Defendant knew plaintiff was involved

CALERON

–continued from page 9–

Respecting the alleged conflict of interest, the judge found that ESA knew Caleron was involved with the adjacent lands. Hence there was no undisclosed interest or secret benefit that would disentitle it to damages.

Justice Nation also rejected ESA's counterclaim for damages due to the wrongful filing of the lien and caveats.

Citing the Alberta Court of Appeal in *Hett v. Samoth* (1977), 3 Alta. L.R. (2d) 97, the judge held that the services of a real estate developer could not maintain a builders' lien. He found that neither was the builders' lien for an amount grossly in excess of the amount due, nor was Caleron aware that it did not have a valid lien.

Caleron admitted at trial that it could not maintain its caveats, as it had not signed the draft agreements. But as the judge found that the caveats were not placed or continued "without reasonable cause," they could not form the basis of compensation under the *Land Titles Act*.

Finally, the judge held that ESA had not shown the project was delayed "solely because of the lien and caveats."

Reasons in *Caleron Properties Ltd. v. ESA Holdings Ltd.*, [2003] A.J. No. 38, are available from FULL TEXT: **2243-023**, 26 pp.

Proposed common issues rejected

RE/MAX

–continued from page 9–

The proposed class definition referred to "all past and present real estate sales persons who entered into contract with Re/Max …" and paid errors and omissions insurance premiums.

Justice Charbonneau observed that although there was no need at the certification stage for exact numbers or the identity of class members, the plaintiffs had failed to supply even their "best information" on the number of members, as required by the Act's s. 5(3).

Counsel for Re/Max argued that the class was not identifiable because there was no evidence that the potential class members truly wanted to participate in the action.

But Justice Charbonneau decided that, for the time being, he should accept that the numbers of salespersons under contract with the defendant varied from 180 to 250 between 1989 and 2000, and that it has been in business for 20 years at eight offices in Ottawa. He ordered that the class should be closed as of the date of the certification order and that the definition should be amended to make reference to Clause 7.

Regarding the need for common issues, he referred to the test in *Carom v. Bre-X Minerals Ltd.* (1999), 44 O.R. (3d) 173: "A common issue must have sufficient significance in relation to the claim asserted such that its resolution will advance the litigation. Furthermore, the resolution of the common issue must advance the litigation in a meaningful way."

He rejected some of the common issues proposed by the plaintiffs, such as that of limitations, as more appropriate for consideration as individual issues. However, he found six issues that met the Act's requirement to advance the litigation in a material way.

As to whether a class action was a preferable procedure, Justice Charbonneau applied the Act's goals of judicial economy, access to justice and behavioural modification to the individual issues involved. He noted that "the main thrust of this litigation is the interpretation of a specific clause in a standard contract entered into by every member of the class" and the fact that the determination of individual damages would be "relatively simple" given that they are "essentially liquidated damages claims."

He concluded that the existence of individual issues "does not diminish the substantial benefits of having the main issues raised by this litigation addressed in the context of a class proceedings."

Finally, as to the ratification of the representative plaintiffs, the judge rejected a defendant's argument that they would not fairly and adequately represent the class members, some of whom still work at Re/Max, because Wilson and Rousseau are working for competitors.

Justice Charbonneau held that a representative plaintiff may work for a competitor without being in a conflict of interest on the common issue. He found that their interest in the lawsuit is the same as those salespersons who still work at Re/Max.

Ottawa sole practitioner John Dempster acted for Wilson and Rousseau. Arthur Cogan of the J. Arthur Cogan Law Office represented Re/Max.

Reasons in *Wilson v. Re/Max Metro-City Realty Ltd.*, [2003] O.J. No. 79, are available from FULL TEXT: **2243-022**, 7 pp.