



# Real estate fraud legislation: shaping the new practice reality

*Prompted largely by extensive media coverage of title and mortgage fraud, the Ontario government last year embarked on extensive consultations with the various parties involved in real estate transactions. Among the issues discussed were: how the land titles system works; who can access it to register title documents; what lenders do before they make mortgage loans; and lawyers' role in the transactions.*

*In the fall of 2006, the Ontario government announced a two-phase program of reform that will reshape residential real estate practice.*

## **Phase one: Taking care of problems**

This first phase was reflected in the Ontario *Ministry of Government Services Consumer Protection and Service Modernization Act, 2006*, released in October 2006 and often referred to as Bill 152.

Phase one focused on:

- increased Ministry ability to suspend and/or revoke electronic registration credentials;
- clarification of the effect of registration of fraudulent documents; and

- clarification that title insurers cannot seek reimbursement from the Land Transfer Assurance Fund (LTAF).

For real estate practitioners, the Bill raises a number of practice issues.

- First is the need to learn the substantive provisions of Bill 152's treatment of fraudulent instruments (found in the provisions which amend the *Land Titles Act*). You can access the most current version of the *Land Titles Act* at [www.e-laws.gov.on.ca/DBLaws/Statutes/English/90105\\_e.htm](http://www.e-laws.gov.on.ca/DBLaws/Statutes/English/90105_e.htm).
- A major practice issue for lawyers is how to reduce the risk that they become a target for the Director of Land Registration to suspend, and potentially revoke, the lawyer's ability to submit documents electronically. These powers were incorporated in the *Land Registration Reform Act* by virtue of the Bill 152 amendments.

The Director has the power to issue an immediate suspension where it is in the public interest or the Director has reasonable grounds to believe that an electronic document is not authorized. When a lawyer receives a notice of proposal to revoke the authorization to register (that is, to make the suspension permanent), the lawyer has 15 days to serve a written request for a hearing on the Director. If the lawyer wishes an oral (as opposed to written) hearing, that must be specified.

#### PRACTICE IMPLICATIONS

From your client's perspective, your suspension could have disastrous consequences in terms of an upcoming closing. You should note that the Director has the power under the Act to withdraw the suspension, pre-revocation, where the Director considers the withdrawal in the public interest. So, don't hesitate to advise the Director immediately if you believe that you have been the target of a suspension by mistake.

For a variety of reasons, it is worthwhile for lawyers who practise in a firm to ensure that at least one other lawyer in the firm has electronic registration credentials. That way another partner or associate would be able to assume carriage of a file on short notice, if necessary. (The definition of "electronic document submitter" in the Act indicates that the power to suspend is on an individual person, not firm-wide, basis. Therefore, it is reasonable to expect that firm members will be able to back each other up this way.)

For sole practitioners, the Joint Committee on the Electronic Registration of Title Documents has long recommended that lawyers have an understanding with another lawyer in the community who could provide assistance in appropriate circumstances. Traditionally this has been discussed in the context of registrations needing compliance with law statements when a sole practitioner is on vacation. However, it could apply where there is need to refer a client on short notice. (Of course, the practitioner agreeing to assist needs to assure him or herself that there is nothing suspicious in connection with the client or transaction being referred.)

If you think that a suspension or revocation may cause a loss for one or more clients, contact LawPRO immediately as those clients may have a potential claim against you, depending on the circumstances.

Do not forget that complying with the Law Society's Residential Real Estate Transaction Practice Guidelines may be the best way to ensure that you never get caught up in this problem.

The Guidelines suggest that you:

- Check the client's identification carefully, retain details of the I.D. presented and get an authorization signed in your favour to make the registration.
- Keep the back-up documentation for any compliance with law statements you make to facilitate the registration.
- Look at the pattern of deleted instruments on title: apply your common sense to what the title of the average client looks like. Does this look different? Don't act where you are suspicious about the client, the circumstances of the deal or your referral source!

#### Phase two: Tightening the ground rules

In phase two, rolled out this spring, the government focused on increasing accountability for access to the electronic registration system and processes, among other things.

One of the major proposed changes will restrict access to the electronic registration system to lawyers for certain document types. Specifically,

- only lawyers will be able to register transfers, and
- registration of a transfer will involve two lawyers, one for the transferor and one for the transferee.

It is expected that there will be very few exceptions to this two-lawyer requirement – the exceptions are still under consideration – but as a matter of principle will likely only include same-party transfers. However, the Ministry of Government Services is prepared to continue the dialogue with the Law Society on this issue in the future, after an initial rollout period.

Many lawyers are surprised that transactions between family members are unlikely to be exempt from the two-lawyer requirement. Unfortunately, there is evidence that in the modern world, identity theft often involves a family member or co-worker<sup>1</sup>. In terms of real estate fraud, there have been high profile cases in Ontario where a family member was the first true victim of the fraud, often because a power of attorney was fabricated or used incorrectly. Spousal impersonation has also been a problem for many years. Further complications arise because it can be challenging to establish the good faith of the alleged victim once a family member, now outside the jurisdiction, obtained significant proceeds from a real estate fraud.

Non-lawyers who meet certain standards of identity, financial solvency and appropriate qualifications regarding character and/or regulatory oversight will be allowed to register mortgages,

discharges and similar documents. As well, lawyers who qualify to register transfers will qualify to register other documents.

The most common question from lawyers is: Why just transfers? Don't many of the reported cases involve fraudulent mortgages?

While that is correct, the Ministry of Government Services has stated that "by restricting the ability to register transfers of land to this group, the main documents involved in title fraud could be isolated, and consumers would be provided with additional protection."

When you think about it, the worst nightmare for the government, and all stakeholders in the real estate industry, is to have two families fighting in good faith over who gets possession of a property. To end up with two consumers at odds over a property, there has to be a transfer somewhere along the way, whether prepared fraudulently in the name of the original owner or as the result of a power of sale based on a fraudulent mortgage. The more lawyers involved in any transfer scenario, the greater the chance the problem will be caught: That is the flattering implication of the government regard for the legal profession. Mortgages, on the other hand, are about money and the defrauded lender can always be made whole with money.

Lawyers should expect to go through a new application process with the Ministry of Government Services later this year, in order to become eligible to access electronic registration in the future. The sooner you get this done, the less chance of disruption to your practice.

## LawPRO's mandatory program evolves: meeting the new challenge

When it proposed to restrict access to register transfers to lawyers, the government also sought to have fraud by a lawyer covered by insurance when it involved registering a fraudulent instrument within the meaning of the *Land Titles Act*. Any lawyer intending to practise real estate would be required to purchase this new coverage, which is to be provided by LawPRO.

LawPRO has proposed to provide this coverage subject to certain conditions. First, to keep premium costs to a minimum – about \$500 per year – the following would be ineligible for applying for this fraud coverage:

- persons who are in bankruptcy;
- persons who have been convicted or disciplined in connection with real estate fraud; and
- those under investigation, where the Law Society obtains an interlocutory suspension order or a restriction on the lawyer's practice prohibiting the lawyer from practising real estate, or an undertaking not to practise real estate.

As well,

- Protection will be limited to the registration of a fraudulent instrument under the Land Titles Act, and not for other types of circumstances involving fraud.

- This protection applies regardless of whether any legal service was ever provided – that is you do not have to have been acting on the transaction that was ultimately involved in the fraud.
- This new coverage would not apply to transactions that occur before the coverage comes into force, nor for claims to which title insurance would apply.
- The sub-limit protection will be \$250,000 per claim/\$1 million aggregate;

So, put simply, when a lawyer is involved in a file where there is a fraudulent registration, there are three possibilities.

- The lawyer could be innocent of any fault. In that case, there continues to be no exposure for the lawyer at common law, nor of the LawPRO program.
- Secondly, the lawyer could have been negligent, in which case LawPRO's standard mandatory coverage would be applicable.
- Thirdly, if the lawyer was involved in the fraud and it involved registration of a fraudulent instrument, the new coverage would come into play.

Note that there can be other types of fraud or theft that do not involve fraudulent instruments. For example, a lawyer could intentionally lie to a lender about the past value of a property based on registered title, in order to help a borrower client. The lawyer eventually registers a mortgage in the lender's favour, but given that the true registered owner of the property appropriately authorized the lawyer to register the mortgage, it is not a fraudulent instrument and the mortgage is enforceable.

In the alternative, a lawyer simply steals money from his or her trust account. In these circumstances the lawyer would not have protection under the new fraud coverage; depending on the individual lawyer's choice of LawPRO options, the lawyer may have innocent party coverage under other aspects of the lawyer's insurance policy with LawPRO.

Title insurers will not be able to access this coverage, just as they are not able to bring claims to the Land Titles Assurance Fund. So, lawyers remain exposed personally to claims from title insurers where the lawyer acts fraudulently; there is no protection for this in the contract between the Law Society and the various title insurers.

Where is the good news in any of this? If real estate lawyers are not the fraudsters, or implicated criminally in the fraud when a fraudulent instrument is registered, LawPRO may be in a position to moderate the premium for this special coverage in future years. As well, under Order ODOT-2007-02 issued by the Director of Titles on May 25, 2007, lenders who want to pursue a claim to the Land Titles Assurance Fund are required to take reasonable steps to verify the identity of the borrower and that the registered owner is, in fact, transferring or mortgaging the property.

With lawyers increasingly on the lookout for suspicious deals, and lenders playing their part, there is reason to be optimistic on the part of all participants in the real estate industry, although fraud in our society will never be totally eradicated.