Real estate casebook: Limitations, undertakings, and getting caught holding the bag

Here we comment briefly on real estate law decisions we've followed this year.

Limitations: Finer points

Limitations law is not as top-of-mind to real estate solicitors as it is, for example, to litigators; but that doesn't mean nothing of interest ever happens. Two recent Court of Appeal decisions have provided clarification of two finer limitations points relevant to real estate practice.

Limitations Act, 2002 and guarantees within a mortgage

In *The Equitable Trust Company v. Marsig*[1] the Court of Appeal was required to determine what limitation period applies to an action to enforce a guarantee contained in a mortgage. In 2005, Marsig signed a guarantee contained within a mortgage. The mortgage went into default in 2007, the plaintiff lender issued a Notice of Sale in late 2007, and the property sold at a deficiency in 2008. On September 17, 2010, the lender sued Marsig on the guarantee.

Marsig sought summary judgment on the basis that the claim was statute-barred. He characterized the 2007 Notice of Sale as a demand, and asserted that this made the guarantee a demand obligation. Demand obligations, he argued, are subject to the two-year limitation period established by s. 5 of the *Limitations Act, 2002*[2].

At trial, Justice Ramsay held that the guarantee did not meet the definition of a demand obligation, and that therefore the applicable limitation period was ten years as provided under s. 43 of the *Real Property Limitations Act*[3].

Marsig appealed. The Court of Appeal accepted (without deciding) the characterization of the guarantee as a demand obligation, but held that since the demand for payment based on the guarantee fell within the definition of "an action upon a covenant contained in an indenture of mortgage" as provided in s. 43(1)(k) of the *Real Property Limitations Act*, it was subject to the 10-year limitation period imposed therein.

Mere contemplation of arbitration won't suspend limitation period

Penn-Co Construction Canada (2003) Ltd. v. Constance Lake First Nation[4] was a case about the construction of a school. During construction, deficiencies arose that ultimately led to Constance Lake terminating the contract and a claim for breach of contract by Penn-Co. In July 2009, more than three years after it first served formal notice on Penn-

[1] 2012 ONCA 235 (CanLII)
[2] S.O. 2002, c. 24, Sch. B
[3] R.S.O. 1990, c. L.15
[4] 2012 ONCA 430 CanLII

Co requiring it to remedy the deficiencies, Constance Lake issued a counterclaim. Penn-Co brought a motion arguing that the counterclaim was statute-barred. The motions judge agreed, and the counterclaim was dismissed.

Constance Lake appealed. It argued that the two-year limitation period imposed by the *Limitations Act, 2002* was suspended when it commenced arbitration of the dispute as provided in s. 52 of that Act.

The Court of Appeal disagreed. There was a history of communications between the parties, dating back to 2005, about how the dispute might be resolved (including a proposal by Constance Lake, on January 16, 2006, that the conflict be resolved via formal arbitration). However, the court found that there was no actual commencement of arbitration within the meaning of s. 23 of the *Arbitration Act, 1991*[5] sufficient to suspend the limitation period under s. 52 of the *Limitations Act, 2002*. It also found that the parties' discussions about arbitration did not create an estoppel preventing Penn-Co from relying on a limitations defence.

For a very useful general primer on *Limitations Act, 2002* jurisprudence, see LAWPRO research director Debra Rolph's casebook on the subject published in the August 2012 issue of LAWPRO Magazine.

Lawyer's undertaking to investigate status of liens not a guarantee of title

In *McLeod & Co LLP v. 1247089 Alberta*[6], the numbered corporation sued the law firms on both sides of a property deal. The deal was for the numbered company's purchase of a partially-completed house from Aspen Land Development.

In the course of the deal, Fooks – a lawyer with McLeod & Co. LLP, the firm representing Aspen – gave an undertaking to a lawyer from Cameron Horne Law Office LLP, the firm representing the numbered company, to discharge three liens from title. Two of the liens were in favour of a company called Lumber King.

Fooks, upon receiving the purchase funds, contacted Lumber King to pay the liens. He was advised that the liens had already been paid. Lumber King provided registrable discharges for both liens. Fooks then released the purchase funds to Aspen without subtracting the amount of the liens, and registered the discharges.

After the deal closed, the lawyers learned that the party that had paid out the Lumber King liens was the purchaser. The purchaser had done so with the expectation that the lien amounts (despite already being paid) would be held back from the purchase money and (double-)paid to Lumber King, resulting in a credit toward ongoing construction work in favour of the purchaser with Lumber King. Instead, the funds went to Aspen and could not be recovered. Aspen went out of business and was judgment-proof. The numbered company purchaser sued both law firms.

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[5] SO 1991, c 17
[6] 2011 ABQB 708

The claims succeeded at trial. The trial judge held that both lawyers owed the purchaser a duty of care: the purchaser's own lawyer, while not negligent in tort, was under a strict contractual duty to ensure that the portion of the purchaser's money intended to cover the liens made it into the hands of Lumber King; and Aspen's lawyer, by giving the undertaking, owed the purchaser a duty of care to accomplish that same result.

The law firms appealed and the appeal was allowed.

With respect to the purchaser's own lawyer, the Court of Appeal held that the contract between the purchaser and his lawyer required the lawyer to obtain clear title to the property. He did that. To hold that there was an implied term that the lawyer would protect the purchaser against loss of purchase monies through no fault of the lawyer's own would be, in effect, to make the lawyer the guarantor of the transaction – he would effectively be absolutely liable for the result, without being able to rely on a defence of due diligence. The court held that a normal lawyer-client relationship, in a real estate transaction, does not create this kind of liability; and that there was no reason to find a special such duty implied in this particular case.

With respect to the liability of Aspen's lawyer, the Court of Appeal rejected the trial court's suggestion that real estate lawyers on opposite sides of a transaction should not be viewed as adversaries but rather as the "facilitators" of the transaction. Fooks undertook to discharge the liens from title, and he complied with that undertaking. As the representative for the party adverse in interest to the purchaser, he owed no duty of care to the purchaser directly; his only obligation was that which arose under "[t]he system of trust conditions and undertakings that forms part of the standard real estate conveyancing protocol in Alberta". The court noted that that system is designed to "safeguard the rights of vendors and purchasers, who are inherently adverse in interest", and that as a result, lawyers are required to strictly comply with their undertakings. Mr. Fooks undertook to discharge the liens, and did so. He owed no duty of care to the purchaser to do anything more.

When a lawyer is instructed to obtain title insurance and doesn't do so, guess who's left holding the bag?

Here at LAWPRO we are often asked why, despite advent of title insurance in Ontario, real estate practice continues to produce such a high proportion of claims against lawyers.

The answer to that question is complex; you can read more about it in our articles "Title insurance: Not the panacea lawyers had hoped for" and "Title insurance: Separating fact from fiction" available at practicepro.ca. But the easiest way to have a title insurance policy fail to cover a claim is not to secure the coverage at all.

We recently closed a claim file in which a lawyer was sued for several hundred thousand dollars in the wake of a mortgage fraud. Was this just one of those bad apples we all read

about in the Law Society's discipline cases – a rare rogue lawyer who places fraudulent mortgages to fund his or her own lifestyle?

No. In this case, the lawyer received instructions from the lender client to obtain title insurance for the transaction. The purchaser/borrower in the transaction was a corporation. The lawyer had performed a corporate search that revealed that the individual requesting the loan was the sole principal of the purchaser company. The lawyer contacted a title insurer to arrange a policy. He neglected, however, to confirm that the policy had in fact been placed before he allowed the closing to proceed. Subsequent to closing, the proposed insurer communicated that it was not willing to issue the policy.

After a default on the mortgage, it was discovered that the individual who had applied for the loan on behalf of the corporate purchaser had no connection to the corporation and was not known to the real principals: The fake principal had, six months prior to closing, registered a fraudulent Notice of Change with the Ministry of Government Services. The police confirmed that the fraudster's name – apparently a fake identity – was known to them.

Upon discovering that, contrary to its instructions, there was no title insurance on the property, the lender sued the lawyer for the amount of the loan.

Counting on title insurance to protect you from fraud-based claims? Make sure the title insurer has bound coverage before releasing funds!