

“Pre-emptive Protection”

Guarding Against Real Estate Fraud: Creating an Operational System in Your Office

“It is said that fraud is a crime of opportunity – weaknesses in systems are exploited and the fraudster(s) profit from our lack of rigour ...

... the best way to prevent fraud is to **believe it can happen to you** and then act accordingly!”

- Ontario Lawyers Gazette

A Paper Presented During “*A Viper in the House: Real Estate Fraud & You*”
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Introduction: “It’s A War Out There!”

Today, transactional fraud has become a going concern – and a growing problem – for real estate practitioners across the Province of Ontario. Indeed, you need only look to recent articles in the Toronto Star, Windsor Star and other local newspapers to note the increased frequency of these occurrences. As the frequency and intensity of fraudulent behaviour heightens across the country, law offices everywhere are tightening their policies and procedures. However, the fraudster – as we all have come to label the “enemy” – has proven him, her, or itself to be a formidable foe. This is a new battle to be waged against an old enemy. New techniques are being developed daily, and make no mistake – even the most attentive lawyer can be fooled. In practicing a clever technique of “guerrilla warfare”, the fraudster usually lies low and out of sight. They will study and test our complex regime of real property law, looking for each and every hole to exploit. The best fraudster is not a copy-cat – their technique(s) is/are entirely original and usually well disguised. We, in turn, can no longer rely on our old and outdated tools when we go into combat. If we do so, we are doomed to failure.

In short, it is the fraudster’s wish to stay ahead of the game. Conversely, it is our wish to prevent this “advance” as best we can. Despite the fraudster’s inevitable originality, we all have a duty to stay vigilant. At the very least, we can slow the fraudster’s push across enemy lines. In the fight against real estate fraud, every lawyer can do his or her part by incorporating a number of simple mechanisms into their practice. The goal of this paper is to help you and try to provide you with practical resources and tools to stop or prevent fraud. It is by no means exhaustive. In fact it is quite limited, and based on my limited ability to interact with the profession and other sources. But it is a start to help you and your colleagues join – and help win – “the war” on real estate fraud. In other words, it will offer some suggestions on how you, the real estate

practitioner, can operationalize a system of protection against fraud in today's most common real estate transactions.

With a bit of planning, your office can create a routine, consistent, and strategic approach to fraud prevention. Will this increase the cost of each file? Absolutely! But it will also ensure that our practice survives and that our "clean" files stay put. Some lawyers have expressed a distain and a disinterest in getting involved in any way in this process. If that is your attitude, then I suggest you start practicing some other form of law. As lawyers, we are the "gatekeepers" to the transaction. We give the Lending Institutions and the Government a good, valid and viable reason to involve us in the whole real estate process. If we absolve ourselves of the responsibility that comes with our role, then there will be no need for us at all.

A Strategic Approach: "The Battle Plan"

For simplicity's sake, this paper will outline a layered strategy for fraud prevention at three separate levels: (1) the client **intake**; (2) the **deal phase**; and (3) the **universal approach**. The strategy itself has been formulated using two sources: (1) various policies and procedures that have been successfully implemented at McTague Law Firm LLP; and (2) an impromptu survey of other real estate practitioners across the province. While certainly not "all-encompassing" it is my hope that by using this system, the vigilant real estate practitioner will be able to identify the possibility of fraud before it has the opportunity to develop into something more dangerous (and expensive!).

Overall, one point **cannot** be overstated: in whatever way you decide to operationalize fraud prevention and detection in your practice, everyone in your office must be – and must stay – on the same page. In other words, you and your team should crystallize a routine. At the very

least, there should be a system of checks and balances in your office. Whether you choose to utilize all of the tools below, or only a few, just remember: this is a decision that may very well make the difference between catching the crook or being caught by one.

A) ***THE INTAKE STAGE*** – When a new client walks into your office, what “defensive mechanisms” should your team have in place?

- i) ***Confirm Your Client’s Identity***: When a new client comes through your door, a member of your staff should complete a “reverse phone-number” search of that person on <http://www.canada-411.com>.¹ This search is absolutely essential, unless you have dealt with the person or corporation in the past. Always insist that your client provide you with a land-based telephone number, because Directory Assistance does not yet support cell-phones. Overall, the person that you designate to conduct this search should do so in order to ensure that the information your client has given you is valid.
- ii) ***Check Your Database & Files***: After your initial search is complete – but prior to accepting a retainer – have a member of your staff crosscheck your firm’s roster of past and present clients. This will indicate whether you have done any work for the person or corporation in the past, and, if so, what type of work was done. Most importantly, this type of search usually “rings a bell” if there have been previous problems or issues with the client. Conversely, this search is also an excellent preliminary tool for identifying a potential conflict of interest

¹ For more information on this and other innovative suggestions which I have found to be helpful, please refer to the Checklist created by Steven Shub, which has been attached at Appendix A.

(should one exist).

B) **DOING “THE DEAL”** – After the retainer has been signed, what other steps can you take during the transaction to ensure that your practice is not being exploited by the enemy?

i) **Take The Lead:**

a) Be an active participant in each and every deal that comes across your desk. Most importantly, before executing any pay-outs to either of the parties, ensure that you personally review any and all Trust Statements that are associated with the deal and with your client.²

b) On matters that are collateral to the transaction, be sure that you consistently encourage the rest of your staff to ask you questions should someone become suspicious or confused. Likewise, always stay in close contact with each member of your team about each file as you move towards the closing.

c) Make it loud and clear in your office that **documentation matters** – if something suspicious arises, it should be documented without delay. As well, ensure that every member of your staff can identify and recognize the overly anxious, nervous or “restless” client. You will find that e-mail is a powerful tool in this respect. It is essential that you foster a policy of immediate communication from the outset: if any member of your staff becomes apprehensive about a file, they should feel comfortable about informing you right away. E-mail has simplified this communicative

² My thanks to Jack Ramieri of Miller, Canfield, Paddock and Stone, LLP, for reinforcing the importance of this step.

capacity even further.³

ii) ***Identification, Take Two:***

- a) To explain the importance of confirming the client's identification, the common example of a mortgage transaction may be used. Prior to completing a mortgage deal on behalf of your client, instruct your staff to take a number of precautions. This cautious approach is necessary to confirm that the information given to you by your client remains properly aligned with what any other parties to the transaction – such as a lender – may desire. It is essential to recognize that your first line of defence sits at the front of your office: train your Receptionist or front line person to request at least two pieces of government-issued identification when the client arrives. When your client makes an appointment, let him or her know that two pieces of identification are required. Not all Lenders require the same form of identification. You are obligated to play by their rules and meet their requirements – after all, it's their money! So, make sure that the client knows in advance what is expected of them. Before they show up at your doorstep.
- b) Have your Receptionist or front line person electronically scan the client's identification. Once this step has been operationalized in your office, use this scanned copy to confirm that the documents

³ For more information about the importance of taking a leadership role in your office, E. Susan Elliott has published an excellent article entitled "Is There a Crook In The Firm?". An excerpt of this article is available on the Law Society of Upper Canada's website at <http://www.lsuc.on.ca/news/b/olg/novemberdecember-2004-vol8-no-6/fighting-real-estate-fraud/>.

provided by the client will satisfy the requirements of any lender(s) involved. Moreover, double-check your scanned document and scanned license against any instructions received vis-à-vis the transaction itself.⁴ If any of the listed names differ, draft and have your client sign a formal affidavit confirming that s/he is who s/he claims to be. You can even go online and determine if a Drivers License is still valid if you suspect a problem. (see Schedule “B”, attached)

- c) A common form of identification provided by most clients is their Ontario Drivers License. For as little as \$100 you can purchase a magnetic strip reader that reads the magnetized strip on the back of their license. It then can be stored with the scanned copy of the other identification provided in your database. For a small fee you can also access the Ministry site and confirm whether or not the License is valid or if there any fines.
- d) For the purposes of further reference, I have attached a “Checklist” created by Steven Shub (see Appendix “A”, attached). Mr. Shub has actively implemented this document into his office’s policies and procedures, and I am advised that he insists his staff follow it closely. Included in the Checklist provided to me by Mr. Shub is a list of 15 items that he demands that his staff watch out for and “flag” if they occur. These are items such as:

- a) Substantial Net Proceeds from the sale;

⁴ *Supra* note 2.

- b) Rush closing;
- c) Not making the sale proceeds payable to the registered owner;
- d) Vacant property;
- e) Is the property mortgage free?; and
- f) The client offers only a cell phone number for contact purposes

These are but a few of the indicia that Mr. Shub has been able to identify as possible “flags” of a fraud being perpetrated. I wholeheartedly agree with his suggestion that if these “flags are raised, we should instruct our staff to take the necessary steps to ensure that we are not unwittingly being dragged into a fraud scheme.” I strongly recommend that you all review the notes that he has so kindly provided.

- iii) ***Avoid Taxation Troubles:*** Prior to closing, the Vendor or the Purchaser (or both) may give you a GST number. As a brief refresher, under the Federal *Income Tax Act*, the Purchaser is obliged to pay (and the Vendor is obliged to collect) GST unless **both** parties have a GST number. In your office, make it a routine to ensure that the number given to you is accurate. Most importantly, this verification search can now be executed online, at the Canada Revenue Agency’s website (<http://www.cra-arc.gc.ca/eservices/tax/business/gsthstregistry/>). Going forward, a member of your staff should be designated to conduct this simple search

as a matter of routine. **Be sure that you have that your searcher print the results as obtained.** Thereafter, place a copy in the client file for future reference.

C) ***THE UNIVERSAL APPROACH*** – Beyond intakes and retainers, what can your office do, on a continuing basis, to identify the enemy and prevent the harmful occurrence of fraud?

- i) ***Train Your Troops***: As we have come full-circle, it is important to reiterate that your staff must be kept “one step ahead” of its enemies in the battle against real estate fraud. Each year, make sure that you send at least one member of your staff to the Law Society of Upper Canada’s (LSUC) annual seminar for Law Clerks. This seminar regularly discusses the “evolution” of the guerrilla warfare we have discussed – and its attendees are always shown new techniques that have developed over the past year, what to look out for, and how to pre-empt their use. When your staff member returns from the meeting, designate him or her as the “team leader” for fraud prevention in your office. Schedule an information-sharing session – led by your team leader – with the rest of your current staff. When a new person comes onboard, have your team leader meet with him or her immediately to discuss the importance of fraud prevention. Overall, “knowledge is power”. If you ensure that this information permeates every level of your practice, your ~~teams~~ heightened level of awareness will translate into a “unified front” in the war on fraud.

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Mobilizing Your “Battle Plan”: Discovering an Anomaly or Fraud

A) *It’s All In The Name* – In Essex County, it is not unusual for the instruction

document to have a different name on it than the actual name of the client. For instance the first name on many Francophone birth certificates will be “Joseph” or “Marie”, as opposed to the names that the client is usually known by or referred to. In practice, I have also seen birth certificates where the client’s name has been recorded as “Sean” or “Jean”, and yet the drivers License has the traditional Christian name “John”. This may be because many people use their second name as their name of choice. There also may be other valid reasons for people using nicknames or pseudo names.

In these situations, it is not good enough simply to ask your client about the discrepancy. Get it in writing. Stop the presses. Ask the client to sign an Affidavit confirming the change of name **and** call the Lending institution to confirm that they are aware of the change or difference. Paper the file to confirm that these parties know about the situation, and ask for a fax confirming that you are safe to proceed. These administrative steps might be a pain to complete, but remember – It’s your livelihood that you are protecting!

B) *Who’s Your Client?* – Keep in mind that not everyone has a Driver’s Licence. In

fact, some of your clients may even lack other forms of identification, which the lending institution has mandated you to obtain in the ordinary course. If your client has no acceptable form of identification, you must get confirmation from the Lender that they are aware of the discrepancy or issue. Call, fax or email the Lender to confirm that they are aware of the problem. Paper the file to confirm they know about

the situation, and ask for a fax confirming that they know of the issue, and that you are safe to proceed.

C) *Gotcha!* – What if you catch a fraudster? Based on personal experience, this is a difficult answer to formulate. As an example, I was recently involved in a transaction where the Purchaser was given a credit on the Adjustments for repairs to be completed. While this type of transaction did raise a red flag, this type of indicia doesn't always lead to a case of fraud – especially if the Lending Institution is aware of it. In the case at hand, it was a requirement of the Lending Institution to get a copy of the Adjustments before the advance. Because a credit for work to be done was recorded in the Offer, I assumed that the Lending Institution had seen the Offer itself. Unfortunately, I assumed wrong! Today, with Mortgage Brokers and other independent individuals involved in many aspects of the transaction you can assume nothing. I am in no way inferring that Mortgage Brokers in dishonest or fraudulent. But, the old method of the client going to the Lending institution; filling out an application and presenting the offer to the institution doesn't always apply.

Once the Lending Institution saw the Adjustments, they asked for a copy of the Offer. I called the Purchaser to confirm that I could do so. I was careful to request instructions in writing from the client for same. If the Purchaser had declined, I would have immediately resigned from the file. As it turned out, the Lending Institution refused to fund the deal and it died. My client, the Purchaser, wasn't happy. However, in the end, what is most important to me was protected – I shielded my practice from a potentially dangerous situation.

Overall, unless you are certain that a Fraud is being committed tread

carefully. However, if you are certain that things are askew, you must act quickly to protect the integrity of your practice. Here are a few helpful hints for getting started:

1. Resign in writing from the file;
2. If possible, get written confirmation from the client that he /she has received a Notice of your resignation;
3. Call the Law Society of Upper Canada;
4. Document everything.

Concluding Remarks and Gratitude

I hope that this paper – combined with my remarks this morning – has suggested to you some practical tips for dealing with, and protecting yourself from, the potential for fraud in the practice of Real Estate law.

Finally, I wish to thank Ray Leclair, and Sally Burks for their comments, ideas and suggestions as to how they deal with Fraud Prevention on a daily basis. Their input and suggestions have been of great assistance in the preparation of this paper. I also wish to thank Eli M. Udell, B.A., M.A. LL.B. for his invaluable time help and dedication in drafting, editing and preparing this paper. His help and commitment to excellence is reflected in its contents.

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Schedule "A"

Suspicious
Circumstances
(Yes/No)

IF THERE WILL BE SUBSTANTIAL NET PROCEEDS (from a sale or mortgage refinance) to be paid to client (who is not using funds to buy and who was not previously known by our office) consider the following matters to help determine whether the transaction might be fraudulent.

- _____ 1. Have we acted for the client before? If so, for what type of matter? A fraudster typically does not return to the same lawyer who did prior file work.
 - _____ 2. Is the closing fast approaching and the client is anxious for the law office to close quickly? A fraudster is anxious to close quickly (to hit and run) so that the innocent duped lawyer who is the tool of the fraudster has no time to think before filling the fraudster's pocket (it is easier than robbing a bank and phony I.D.'s are easy to purchase) The fraudster's own picture and signature will usually appear on the phony I.D. which will reflect another name.
 - _____ 3. Has it been determined that the client is agreeable to make the net sale proceeds payable to the registered owner? Typically, a fraudster wants net proceeds payable to third parties. The question of how net proceeds are to be paid upon closing, being ONLY to the registered owner, should be discussed with the client when contemplating the opening of the file.
 - _____ 4. In a sale, can the listing realtor confirm that there was a FOR SALE sign on the property or if a private sale was it a "cooked" sale or was there a for sale sign on the property with the vendor actually living at the property or was the property vacant or "tenanted".
 - _____ 5. Does 411.ca confirm the reported client address as connecting to one of the client's telephone numbers?
 - _____ 6. Is the "client" only offering a cell phone for contact or are there other residence and business contact phone numbers that can be verified by 411.ca? A fraudster typically is a "hurried business person" (always on the go) and only wants to be contacted on a cell phone. No sale or refinance matter can be accepted into our office where a client will only provide one phone number being a cell phone.
 - _____ 7. If the transaction is a rush closing, has the client referred to unhappiness with prior lawyers and if the job is done efficiently, more business to follow? Fraudsters often like to dangle a "carrot" of future business coming if the innocent duped lawyer acts as an efficient tool of the fraud artist.
 - _____ 8. Is a power of attorney being used and, if so, why? Has the donor of the power of attorney provided a clear copy of a photo I.D. with a currently dated and signed note that the power of attorney is still valid for the intended purpose and enclosing a contact telephone number? Has the donor of the power of attorney been contacted to verify the facts? Does the signature on the note from the donor (confirming that the power of attorney is still valid) reasonably look like the signature in the power of attorney?
 - _____ 9. If a private sale was the deposit paid to the seller's lawyer in trust? If so, was the lawyer contacted to verify this? If payable to the vendor direct, watch out! Do not be comforted in a private sale transaction where the deposit was in fact paid to the vendor's lawyer in trust since there have been several fraud situations where this was done by the fraud artist in order to add legitimacy to the appearance of the transaction. In fraudulent private sales, usually the vendor (impersonating the real owner with a phony I.D.) and the purchaser (also using a phony I.D.) are co-conspirators, each using a different innocent duped lawyer as a tool for "purchaser" and for "vendor".
 - _____ 10. If independent legal advice is needed for a spousal consent has it been noted (as part of the pre-closing processing) to phone the lawyer giving the I.L.A. to confirm he is or has done so? There have been cases where the signed consent and the I.L.A. were fraudulent.
 - _____ 11. Is the property mortgage free or in the last six months has the last security been discharged according to deleted instruments in the parcel register? If so, one might want to confirm with the lender that the discharge was legitimate. If the property is mortgage free, order a copy of the parcel to reveal the deleted instruments so that a clearer picture of the recent history of action on title can be revealed. (even on a sale transaction where there is no mortgage and suspicions have been aroused)
 - _____ 12. For refinancing, does the parcel register reveal that a non-builder title transfer was registered within the last 12 months for a considerably lower price than the current sold price. If so, how does the client justify the sudden increase? Is the new mortgage lender aware of the sudden increase? Disclosure by fax to the mortgage lender of recent price increase is now a requirement by most mortgage lenders.
 - _____ 13. Is the client capable of providing all usual documents including survey (if a non condo) and property tax bills?
- NOTE: If suspicions are raised due to at least three items of concern, determine whether the title insurer (if refinancing) should be advised; whether to discuss the matter with another lawyer in the firm; whether to contact the "client" through any other telephone number available from 411.ca or the white pages of the telephone directory in order to ask a series of questions which might make a fraudster nervous or provide comfort if the client is legitimate' strategy for taking extra care when checking photo on photo I.D. upon sign-up of client and comparing signature on documents to signature on photo I.D.

*** When a deal becomes suspicious on a sale or refinance, create a SUBFILE called "SUSPICIOUS CIRCUMSTANCES" and insert this form as an analysis checklist and consult STEVE