

February 2007

## LAND FRAUD

Title fraud has certainly become a hot-button issue in the last 6 months. However, we have been encountering it for the last 6 years. Since many of our readers, who are employed in debt collection, are also homeowners, we thought that a quick summary of the cases and the latest legislation would be of interest. We had previously discussed this topic in our April 2006 newsletter, but we have updated the discussion and added some views from a different perspective.

### Jaing

We start our overview with the Toronto-Dominion Bank v. Jaing, a 2003 decision of the Ontario Superior Court of Justice. We know it well because we acted for TD.

A fraudster fraudulently transferred a condo unit from the owners to himself. A few months later, fraudster mortgaged the property to TD for \$200,000. A solicitor acted on behalf of fraudster and TD. The solicitor did nothing wrong; fraudster had two pieces of ID in the name of Jaing, the name by which he took title and gave the mortgage. We only discovered the fraud when we attempted to secure the property and found that the real owners still lived in the condo and our fraudster never did.

We knew that if TD and the owners made a joint application to the Land Titles Assurance

Fund, we would lose. We had seen other decisions in which mortgagees attempted – unsuccessfully – to have the Fund indemnify them. The Deputy Land Registrars, who tried the applications, took the view that if a financial institution was involved, it should have better investigated the mortgagor.

Accordingly, we ignored the Fund and commenced an action against the owners for possession. We were successful. The judge relied on a line of cases that stated the following: an original transfer that is fraudulent is void; however, a subsequent mortgage that was signed by the person who was shown on the title register as an owner was valid. The purpose of this reasoning, and the Land Titles Act from which it evolved, is to ensure that people and institutions can rely on the register when carrying out their land transactions. Accordingly, the transfer from the owners to fraudster was set aside – since the owners never signed the fraudulent transfer. However, the mortgage from fraudster to TD was valid – because fraudster was shown as the owner on title at the time and properly gave the mortgage.

Of course, we did not want to have the owners evicted and we told the judge exactly that. We undertook to give the owners as much time as they needed to make application to the Fund for reimbursement of the loss that they suffered due to the fraud.

That process took approximately two years. However, in the end, knowing that TD already had a judgment against the owners, there was little the Deputy Registrar could do, other than pay the mortgage debt. Ultimately, TD received the total amount owing including interest and costs. The police did nothing about it, the fraudster got away with the crime, and the people of Ontario paid.

### Liu

In Household Realty Corp. v. Liu and Chan, a 2005 decision of the Ontario Court of Appeal, the court was faced with a different scenario. Husband and wife owned a property. Husband spent much of his time abroad. During the time he was abroad, wife indulged in her gambling habit and lost. Ultimately, she forged husband's name on a power of attorney and used that power of attorney to place two mortgages on the property. The mortgages went into default and husband was welcomed home with mortgage actions. This case exemplified the maxim "hard decisions make bad law".

The court analysed the power of attorney, as we would have, by saying that its execution meant nothing. Whether the mortgages were executed fraudulently or were executed by way of a fraudulent power of attorney was not relevant to the analysis.

The classical analysis would have stated that the mort-

gages were invalid because they were fraudulent. The court disagreed; it interpreted the Land Titles Act provisions and concluded that the provision that allowed people dealing with land to rely on the register trumped the provision that stated that a fraudulent instrument is void.

Accordingly, the court held that the mortgages were valid against both wife and husband. We think that the court simply did not want to allow wife to have any benefit from her own fraud and, therefore, went out of its way to ensure that would not happen. We are of the view that the court could have achieved the same, or almost the same, result by validating the mortgages only against wife's equity in the property. In that way, depending on the money loaned compared to the value of the property, wife's equity would be wiped out and husband's equity would not.

## Rabi

The fraud in Rabi v. Rosu, a 2006 decision of the Ontario Superior Court of Justice, dealt with a variation of the Jaing fraud. Fraudster1 impersonated the owner. In transactions that took place one after the other, fraudster1 sold to fraudster2 and fraudster2 mortgaged the property to the Toronto-Dominion Bank. The fraudsters used the same lawyer to act for both TD and them and presented forged ID.

The main difference between Rabi and Jaing was that in Jaing, there was no title insurance and in Rabi, there was. In Jaing, TD was the plaintiff in its own right and we, as TD's law-

yers, were mindful of any negative publicity. In Rabi, the title insurers commenced the action in TD's name and appointed the lawyers. The lawyers, it seems, cared not a whit about any negative publicity for TD, presumably because TD was not their client. According to the solicitor who represented the defrauded owners, the solicitors for the title insurers took the position that the mortgagee was entitled and intended to take immediate possession; the title insurer would do nothing to help the defrauded owners.

The judge had a choice. Follow the court of appeal's decision in Liu - resulting in the eviction of the defrauded owners - or use and amend the classical analysis in Jaing. The judge chose the latter. He attempted to distinguish Liu by saying that the facts were different because one of the owners in Liu was involved in the fraud and neither of the owners in Rabi was involved. This, of course, ignored the court of appeal's analysis and was simply an artifice to ignore a bad decision. He then used the classical analysis, but added a caveat. The innocent person relying on the register had to have done so with due diligence in underwriting and effecting the mortgage.

The judge held that TD's underwriting procedures were inadequate to ward off fraud. TD delegated the deal to a mortgage broker; it was not alerted by the failure of the transfer to include parking and storage, by payment of \$30,000 to the mortgage broker, and by the absence of a

deposit; and, most importantly, it authorised a drive-by appraisal rather than insisting that the appraiser actually visit the premises.

Accordingly, the judge held that TD could not rely on the land register because it "*did not even perform rudimentary due diligence and had notice of irregularities.*"

The upshot is that the title insurer paid TD, but was unsuccessful in its bid to recover that loss from the owners. However, TD suffered a whack of bad publicity - all because the lawyers and their title insurer client were not sensitive to the plight of the owners.

Will the banks change their procedures to tighten up on fraud? We do not know. The suggested procedures have costs attached (e.g. an actual inspection is far more costly than a drive-by appraisal) and the mortgage industry is cost conscious and competitive.

## Zivic

In Home Trust Co. v. Zivic, a 2006 Ontario Superior Court of Justice decision, a home owner leased her house to fraudster1. Then fraudster1 fraudulently transferred the property to fraudster2 and fraudster2 simultaneously mortgaged the property to Home Trust. Under these circumstances, even an at-home appraisal would not have caught the fraud because fraudster1 was physically present in the house.

This decision was released after Rabi, but made no mention of it. Rather than using the Rabi analysis, the judge de-

cided that because the transfer and the mortgage were completed at the same time, Home Trust had not relied on the land register. Accordingly, the judge held that, as between two innocent parties, Home Trust ought to bear the loss. She used reasoning akin to that used in Rabi and said "*Such a determination is consistent with maintaining the integrity of the Land Titles System but it also places a greater burden on the mortgagees who had an opportunity to be more vigilant with respect to the transaction they entered into.*"

This reasoning would not have affected the result in Jain because the transfer and mortgage were not registered one after the other. There was a gap of a number of months.

## Lawrence

The trial decision of Lawrence v. Wright, a 2006 Ontario Superior Court of Justice case, was delivered after Liu and before Rabi. The judge in Lawrence, faced with similar facts, felt obliged to follow the Liu decision. The defrauded homeowner appealed that decision to the Ontario Court of Appeal and the lawyer acting for the homeowner, who also acted for the homeowner in Rabi, persuaded the Chief Justice to have the matter heard in front of a five-member panel of the court, rather than the usual three-member panel. At that hearing, the lawyer argued that the court should overrule the Liu decision as a precedent. The lawyers argued the case in late November 2006, but the court has not yet rendered a decision.

## New Act

By way of the Ministry of Government Services Consumer Protection and Service Modernization Act, 2006 (what a mouthful), the legislature amended a number of statutes, including the Land Titles Act. Pursuant to the amendments, the following changes have taken place:

1. The Fund is now a fund of first resort, rather than last resort. Previously, applicants applying to the Fund had to demonstrate that they had done everything possible to collect their loss. This would include an action against the fraudster, collection proceedings to recover the proceeds of a judgement against the fraudster, an action against the lawyers if there was any negligence, and an action against the mortgagees. This was a

very onerous burden to place on a homeowner. Now the Fund is being treated almost as insurance and has been made much more applicant friendly, although the applicant must still show due diligence.

2. Section 78 of the Act is now clear that fraudulent transactions are ineffective. However, instruments subsequent to the fraudulent instruments, when made in good faith and without notice, are still effective (i.e. the legislation reflects the classical analysis).

At this time, we cannot determine the effect of the due diligence requirements set out in the Rabi decision, in a dispute between a subsequent mortgagee and a defrauded homeowner. The concept may be irrelevant because of the changed nature of the Fund, but we will have to wait and see.

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