

February 2008

## FRAUDBUSTER

Who you gonna call to ensure that there is no land fraud? The fraudbusters, of course. They are, specifically, a lawyer or a mortgagee - whether they want to be fraudbusters or not. That is the conclusion in Reviczky v. Meleknia, a 2007 decision of the Ontario Superior Court of Justice.

### The Players

Owner of unoccupied land and building – 88-year-old man.

Fraudster – purportedly a donee under a power of attorney from the owner. The POA was forged. The fraudster sold the land to an innocent purchaser.

Mortgagee – the financial institution to whom the innocent purchaser mortgaged the land when he purchased it.

Fraudster's solicitor – the lawyer for the fraudster on the sale. The lawyer did not know that his client was a crook.

Mortgagee's solicitor – the lawyer for both the mortgagee and the purchaser.

### The Game

The owner discovered the fraud when he checked the property and found a hydro bill addressed to the purchaser. Ultimately, the purchaser agreed that the transfer was fraudulent and the transfer was set aside. The fight was whether the mortgage was to be set aside.

The mortgagee analysed

the problem as follows: the purchaser was an intermediate owner; it mortgaged the land to the mortgagee who was therefore a deferred owner; consequently, since the mortgagee never dealt with the fraudster, the mortgage is indefeasible (i.e. the owner gets his land back, but the land is still encumbered by and subject to the mortgage).

The application was between the mortgagee and the owner, but the fraudster's solicitor intervened and the mortgagee's solicitor provided his entire file. We assume that the mortgagee's solicitor was not financially interested in the outcome because the mortgage was title insured. Conversely, the fraudster's solicitor was financially interested. We have no doubt that if the mortgage was held to be valid, the owner would have commenced an action against the solicitor, alleging that he had a duty of care to the owner to ensure that the fraudster's power of attorney was valid.

### Fact Findings

The mortgagee's solicitor knew that someone was purporting to sell the land under a POA, but initially knew nothing of its form, content, or validity and took no steps to learn about them. The mortgagee also knew that a POA was involved because the agreement of purchase and sale referred to it.

The judge reviewed the mortgage commitment and, because the mortgagee was able to refuse to advance the mortgage funds if it found that the purchaser did not have good title, the judge inferred that the mortgagee "*knew ... of the risk of the purported vendor not being the true owner of the property.*" However, the fact that the commitment was attempting to release the mortgagee from any contingency that it could envisage, hardly meant that the mortgagee knew about the risk for this transaction.

Just before closing, the fraudster's lawyer registered the POA and gave a copy of it to the mortgagee's lawyer. The POA had only one witness and, accordingly, was not executed in accordance with the requirements of the Substitute Decisions Act. Certainly, the fraudster's lawyer had not witnessed it.

### Decision

The judge held against the mortgagee on two grounds.

First, he noted that the same solicitor acted for both the mortgagee and the purchaser and that the solicitor of the fraudster dealt with the solicitor of the mortgagee/purchaser. Since the solicitors were the agents of their clients, he reasoned, therefore the mortgagee dealt with the fraudster. As a result, the mortgagee was not a final owner, untouched by the fraudster; it was an intermediate owner whose charge was defeasible (i.e. as

between the owner and the mortgagee, the mortgage is set aside).

We have problems with this analysis. It creates a relationship from a relationship that never existed and never was envisaged. Since the mortgagee never contracted with the fraudster, to attribute knowledge to it, relying on agency principles, is stretching the agency concepts.

Second, the trial judge found, in his interpretation of prior cases, in particular Lawrence v. Maple Trust a 2007 decision of the Ontario Court of Appeal (see our April 2007 newsletter), that the real question to be answered was not whether the mortgagee dealt with the fraudster, but whether the mortgagee had the opportunity to avoid the fraud. This, he felt, was not just an important question; it was determinative.

As it happened, this was not the overriding test in Lawrence. It was but a reason for the Court of Appeal to create the test that it did create (i.e. if an innocent party dealt with the fraudster, then the innocent party could not simply rely on title).

The judge then held that the mortgagee failed the test implicit in his question. It had the opportunity to avoid the fraud. The mortgagee's solicitor, and through him the mortgagee, should have, he said, questioned the fraudster's solicitor as to how the power of attorney arose and why the power of attorney only had one witness. Also, the mortgagee or its solicitor could have insisted that the fraudster's solicitor contact the owner. The judge reasoned that if the mort-

gagee and its solicitor had done their jobs, the fraudster would have been questioned, would have felt the heat, and would likely have abandoned the fraudulent scheme.

The judge did not make his decision based on the fact that the POA only had one witness. The validity of the POA was not the issue. The issue to him was whether the mortgagee's solicitor should have questioned the fraudster's solicitor or the donor and whether, had he done so, that would have prevented the fraud.

## Now What

Assume that the POA was not seemingly invalid on its face. What does a mortgagee's solicitor do when there

is a POA? Must the mortgagee's solicitor requisition proof of validity of the POA? If so, what is sufficient? Does the vendor's solicitor have to swear an affidavit indicating that the solicitor performed certain tasks to ensure that a POA is valid? Is the vendor's solicitor now an insurer? This decision has discarded previous conveyancing practices. Now, there has to be sufficient investigation to satisfy the solicitors for both parties that the POA is valid.

Given that one of the reasons that the mortgage was held invalid was because the mortgagee had the same solicitor as the purchaser, does this mean that mortgagees will, in all residential situations, now demand that they have separate legal representation? If so, we can see an increase in and duplication of legal fees to the purchaser.

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