

TITLE FRAUD

Is Title Fraud a Problem?

A number of years ago when title insurance companies came to town I recall attending a seminar and one of the selling features of title insurance was the coverage in the policy for fraudulent activity. I also recall at that seminar expressing the view to the presenters that this was not one portion of the policy which would be needed and, if we could have that provision dropped from the policy, would there be a reduction in the policy fee. I am thankful that it wasn't possible to carve out the fraud coverage in the policy, as it is becoming a major portion of claims paid out by title insurance companies. Mortgage fraud now accounts for approximately 40% of claims being paid, as opposed to approximately 15% in the year 2000. Make no mistake, title fraud is becoming a major headache across the country. I suggest that the advent of electronic registry systems, hot real estate markets, virtual lenders anxious to pump the money out to the clients, and pressure placed by clients on lawyers to close transactions quickly, result in less due diligence.

It has been estimated that mortgage fraud is now accounting for approximately 1.5 billion per year in fraudulent activity. South of the border in the United States the FBI had 4000 complaints around the year 2000 and now exceeds 20,000. In the United States, major banks are required to report suspected cases of fraud. In Canada there is no requirement on banks to report fraud and the police indicate that there is a reluctance on behalf of banks and lending institutions to report fraud. Police suggest that banks are reluctant to report fraud because of various funding mechanisms set up to cover land title errors, mortgage insurance with CMHC and a general

reluctance to admit that there is a problem. Consequently, the numbers in Canada could be much higher than estimated. In those cases of fraud which have been investigated, the police report that the fraudsters are linked to organized crime, are becoming increasingly sophisticated, highly organized and looking for easy targets.

How Does It Happen:

1. **Impersonation** - Some fraudsters impersonate the lawyer, arrange the refinancing, obtain the mortgage funds, the mortgage never gets registered, stays current for a number of months and then falls into arrears. In these cases the bank is clearly out of pocket the money.
2. **Lawyers engaged in fraudulent activity** - In Ontario there are approximately 100 lawyers under investigation for suspected participation in mortgage related frauds. This behaviour is not new and covers a whole range of activities from failing to payout mortgages, to participating in Oklahoma flips, and various other sundry activities designed to defraud the mortgage companies. The Law Society of Ontario reports that there has been approximately \$5,000,000.00 per year in investigation costs alone for lawyers suspected of fraudulent activity.
3. **Spousal Fraud** - There are a number of frauds occurring in Atlantic Canada involving one spouse forging the signature of an absent spouse on mortgage documents.
4. **Oklahoma Flips** - This type of fraud involves multiple transfers and refinancing above

the fair market value by using inflated appraisals.

5. **Impersonation** - By far the most highly publicized fraud we are seeing involves fraudsters impersonating the owners of property, fraudulently transferring the title and mortgaging the properties to unsuspecting lenders and purchasers.

The Law

If we have a client who is a victim of title fraud, does the true owner of the property lose or do the unsuspecting purchasers and mortgage companies who rely on the fraudulent conveyances lose? This question looms large and an examination of a recent decision on Ontario serves to amplify the competing interests and their requirement to proceed carefully.

A recent decision out of the Ontario Court of Appeal in Lawrence v. Maple Trust Company 2007, ONCA 74 is directly on point. The court in the Lawrence case was called upon to decide whether the true owner who was the victim of the fraud should lose or whether Maple Trust, the mortgage company who innocently relied on the fraudulent registrations, should lose. In the Lawrence and Maple Trust case, as the court noted, this was a ..."contest between two innocent parties - the home owner and the lender of mortgage monies - who wins?"

Background

1. Susan Lawrence owned her own home in Toronto subject to a mortgage in favour of TD Canada Trust.

2. An imposter posing as Lawrence retained a lawyer to sell the home using a forged Agreement of Purchase and Sale and sold it to another imposter for \$318,000.00. The imposter purchaser applied to Maple Trust for a mortgage and the funds were advanced to the imposter purchaser. The unsuspecting lawyer then registered the mortgage against the property and the TD mortgage was discharged. The TD mortgage discharge was in the amount of approximately \$120,000.00 and the new mortgage in the approximate amount of \$290,000.00, for a net increase of approximately \$170,000.00.
3. The Maple Trust mortgage fell into arrears and they commenced foreclosure proceedings.
4. Lawrence brought an application to the courts to have the transfer and Maple Trust mortgage set aside. The judge had no difficulty setting aside the transfer to the fraudulent purchaser, as it had been procured by fraud. However, the court refused to set aside the mortgage because of a previous decision from the Ontario Court in Household Realty Corp. Limited v. Liu (2005), 261 D.L.R. 4th 79. In the Household Realty case, the court analyzed the provisions of 78 (4) and section 155 of the Land Titles Act, R.S.O.

1990, c 1. Section 78 (4) states:

When registered, an instrument shall be deemed to be embodied in the register and to be effective according to its nature and intent, and to create, transfer, charge or discharge, as the case requires, the land or estate or interest therein mentioned in the register.

Section 155 states:

Subject to the provisions of this Act, with respect to registered dispositions for valuable consideration, any disposition of land or of a charge on land that,

if unregistered, would be fraudulent and void is, despite registration, fraudulent and void in like manner.

The court in Household Realty held that section 78 (4) overrides section 155 and the mortgage holder was entitled to rely on the title documents at the Registry and consequently the mortgage was held to be valid against the innocent owner's property. The court in the Lawrence case then had to decide whether the charge against the property was valid and enforceable against the true owner, in spite of the fact that it was acquired by fraud. At common law, in the absence of any legislative provisions, the Maple Trust mortgage was void because the fraudster purchaser could not give any better title than they had and because they did not have title, they could not pass title to the bank. Maple Trust argued that because of the provisions of 78 (4), they were entitled to rely on the registry records and should be able to enforce their mortgage. The court conducted an extensive examination of the law and concluded that the previous decision in the Household case was wrongly decided and found in favour of the home owner. The court conducted an extensive analysis of the law and decided on the principle of ..." immediate indefeasibility..." and the theory of ..."deferred indefeasibility...". The court found that an intermediate owner, being the person who acquires title from the fraudster, holds a deferred indefeasibility and because the intermediate owner is the person who has the opportunity to detect the fraud, that person is not protected by the provisions of the Registry Act and title vests in the owner who was the victim of the fraud. The court then found that any person who purchases from the intermediate owner is then defined as the "deferred owner" and because that person had no opportunity to detect the fraud, the deferred owner is protected by the Registry Act and acquires good title against the person who lost the property to the fraudster.

Based on that analysis, then if an innocent purchaser purchases a property directly from a fraudster, that person will be classified as an intermediate owner and will lose title to the true owner, but should that person sell to another innocent party, who will then be classified as the deferred owner, that person will acquire good title against the true owner. To my knowledge, this principal has not been tested in light of our own Land Registration Act and it remains to be seen how the courts will deal with such an issue. Regardless of who the court finds to be the true owner or the state of the title, presumably section 85 (1) of our Act will provide compensation to an innocent party. This section states that:

85 (1) A person who sustains loss through a registration, a revision of registrations, a recording or a cancellation of a recording that are not authorized by this Act, or through the failure to revise a registration or to make or cancel a recording, as required by this Act, is entitled to compensation for the loss sustained.

In summary, it has been suggested to me that our region is ripe for title fraud and we should all endeavour to exercise great care and due diligence when dealing with any situations that seem unusual or out of the norm. There is less heartache and headache involved by early detection rather than entering the uncharted waters in the Land Registry Act.

Respectfully submitted,

Blair MacKinnon