

Fraud-proof your practice

Sophisticated (and not so sophisticated) criminal schemes to defraud mortgage lenders and registered owners of their money and real property interest are becoming more prevalent. Real estate lawyers are traditionally used to looking for title problems, survey issues, zoning concerns and other possible glitches in legitimate deals.

But what about fraud? What can lawyers do to immunize themselves and their clients?

Awareness is the key. Real estate lawyers today need to know what kinds of fraud are out there, learn the warning signs, and use the tools that are available to protect against them. Complete prevention is impossible, because criminals will always come up with new methods as their old ones become outdated. But with the proper tools in hand, real estate lawyers can spot many intended frauds before they happen.

First, know the two common types of fraud:

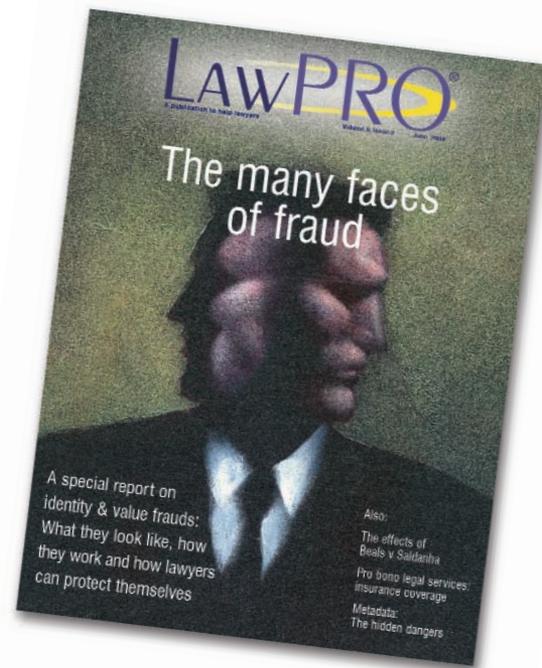
- **Identity fraud.** In this scenario, the fraudster impersonates the registered owner of real property, and transfers it either to him/herself, a person who is complicit in the fraud, or an imaginary person. The same thing can occur when fraudsters impersonate the directors, officers or shareholders of a corporation that owns real property.

The fraudster mortgages the property, forges a discharge, and re-mortgages

it to another lender, each time retaining the proceeds of the mortgages. This cycle can occur several times with the same property before the fraud is discovered. By that time, the fraudster and the mortgage money are long gone.

- **Value fraud.** A property is "flipped" one or more times, at ever-increasing prices, to imaginary purchasers, or persons complicit in the fraud. The final Agreement of Purchase and Sale is at a price much higher than the real value of the property. This Agreement is presented to a lender, which relies on the price to grant a large mortgage on the property. The mortgage typically goes into default soon after closing. In these cases, the lender receives a valid mortgage, but cannot sell the property for enough to recover its investment. The mortgage covenant is typically worthless.

Sophisticated fraudsters combine these two methods, with results disastrous to *bona fide* owners and mortgage lenders.



Warning signs

Lawyers and their staff need to be on the lookout for several "danger signals" which may indicate that the transaction is not as it appears. Some of the most common are:

- A new client, who seems to be involved in many real estate transactions, and promises more business if this deal is closed quickly;
- A client who cannot produce utility bills, tax bills, a survey, or any other documents relating to the property, except the transfer to herself, but will not allow you to contact the lawyer who acted when she acquired the property;
- Municipality or utility companies with no record of your client as the owner of the property.
- A client who is not concerned about higher than normal legal or brokerage fees, or the interest rate of the mortgage;

- An Agreement of Purchase and Sale with no agent, or the name of an agent who never contacts you about the deal;
- An Agreement of Purchase and Sale with no handwritten amendments;
- A direction to pay funds from your trust account to a third party who has no apparent relation to the transaction;
- A small deposit, or a deposit paid directly to the vendor instead of a real estate agent or lawyer;
- Large credits to the vendor on the Statement of Adjustments, for “renovations” or other alleged improvements to the property;
- Instructions received from a “mastermind” who appears to control the transaction, although he/she is not a party to it; and
- The use of counter cheques for post-dated mortgage payments, pre-authorized debits, or otherwise in connection with the transaction.

Although not exhaustive, this list does highlight some of the most common characteristics of fraudulent deals.

Where any of these warning signs appear, obtain more information before closing. If the deals are legitimate, clients should not object to providing this information. In a world where you can't rent a DVD or get a library card without elaborate precautions, clients will see the sense in doing this when hundreds of thousands of dollars are at stake.

Law firm staff can be valuable tools in identifying possibly fraudulent deals. Often, they receive the Agreement, open the file, and review the search before you do. If they know the warning signs and look for them, they will be able to draw your attention to possible problems early in the deal.

Title insurance: fraud protection

Most title insurance policies, including those offered by TitlePLUS^{®1}, First Canadian, and Stewart Title, provide coverage for pre- and post-closing fraud.² Each has underwriting requirements that are designed to detect and prevent fraud. These may include, for example:

1. Obtaining, reviewing and copying photo identification for clients not personally known to you. This applies to mortgage and purchase transactions, including purchases for “cash” (with no mortgage);
2. Advising the title insurer of the date and price of any arm's length transfer of the property within a specified time period; and
3. Requiring a search of automated titles for deleted instruments, and advising the title insurer of all instruments registered within a specified period before the closing date.

Many lenders also have anti-fraud requirements, which must be complied with before they will advance funds.

“Existing owner” policies

Often, homeowners who did not buy title insurance (or bought their houses before residential title insurance was generally available) hear “horror stories” about real estate fraud, and want to protect their properties. Although the likelihood of fraud affecting a particular property is probably small, title insurance is an inexpensive way to put owners' minds at rest. A variety of title insurers now offer these policies³.

Fraud is a serious risk in real estate transactions, and all indications are that it will remain so in the future. Stay up to date on the most recent fraud stratagems and warning signs as they develop, and train your staff about them. Numerous resources are available for this purpose, including continuing legal education programs for lawyers and staff, legal publications, and websites such as www.lawpro.ca/magazinearchives.

With lawyers and their staff alert to the warning signs of fraud, and how to protect their clients against it, the bar can hope for a future when more potential fraudsters are deterred from attempting real estate fraud.

Lisa Weinstein is underwriting manager with LAWPRO's TitlePLUS program.

¹ TitlePLUS is the registered trade mark of Lawyers' Professional Indemnity Company.

² See the policies for details of coverages and exclusions.

³ Title insurers may have different underwriting requirements for these policies. For details, contact them.