



Identity Theft

Mortgage Mayhem

Peter Bowal

"The challenge for a Legislature and for us in giving advice or comments about this is in trying to decide how you treat those interests, because there are going to be people hurt no matter what happens."

— Ontario, Legislative Assembly, *Official Report of Debates*
(Second Session, 38th Parliament, 4 December 2006)

Dubsanka Zivic was the registered owner of a house and lot in Toronto. In 2004, without her knowledge, ownership of this property was transferred to Emil Bakiashvili who then quietly used the title documentation to secure two mortgages, totaling close to a half million dollars.

The object of this type of fraud is not to steal land. Rather, it is to steal money from lenders. There are two types of mortgage fraud. *Value fraud* schemes, which will not be discussed further in this article, artificially inflate property values to dupe mortgage lenders. In *identity fraud*, of which Ms. Zivic was a victim, the fraudster impersonates the true property owner. The fraudster forges the owner's signature in sale documentation filed at land registry offices to deceitfully obtain ownership on paper. He or she then sells the land to another rogue or uses that property to obtain money through lines of credit or mortgages from unsuspecting lenders. The

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imposters abscond with the money and the mortgages immediately slide into default. The innocent owner, who knew nothing of what was happening, and lenders, who relied upon the officially registered documentation, look to each other for compensation.

Ontario's *Land Titles Act* does not solve this problem. Section 78 confirms that a transfer or mortgage is effective when registered. This suggests that fraudulent documents can create valid interests in a real property upon registration. However, section 155 of the Act confirms that a fraudulent transfer or mortgage is void.

The land titles system is based on three principles which comprise the doctrine of indefeasibility of title: the mirror, curtain, and insurance principles. The mirror principle says the register is the mirror of the title. The curtain principle means the purchaser and mortgagee can rely on the face of the register — they do not need to research past dealings with the land. The insurance principle holds that the province must compensate anyone suffering loss resulting from the register's inaccuracy.

Immediate indefeasibility proposes that once a fraudulent document becomes registered, it cannot be annulled. The fraud occurred prior to registration. At this point, the

only recourse for injured parties is to apply to the insurance fund for compensation. By contrast, the concept of *deferred indefeasibility* means that an innocent owner maintains property rights. While the fraudster does not immediately obtain title, innocent lenders dealing with the fraudster do have valid property interests.

This technical legislation must be reconciled with the long-standing common law real property rules that a fraudulent transfer cannot create a legal title — *a person can convey no better title than he had* and *the registration of a void document cannot cure its defect*.

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Judicial Response

While landowners essentially have no opportunity to discover that their property is being fraudulently sold and mortgaged, much less to prevent the fraud, several recent judicial decisions have applied the concept of deferred indefeasibility. In *Household Realty Corp. v. Liu* (2005), Ms. Chan forged her husband's signature to three new mortgages when he was out of the country on business for extended periods of time. This enabled her to obtain additional mortgages on a property she jointly owned with her husband. She forged his signature on a Power of Attorney and then used it to register a mortgage from a bank. The Ontario Court of Appeal held that the bank and a subsequent lender, neither of which participated in the fraud, were *bona fide* mortgagees for value and their mortgages were valid. The property was therefore subject to the mortgages even though Ms. Chan's husband had not signed them.

A similar case of fraud within a family was *Dhillon v. Dhillon* (2006). Mrs. Dhillon

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fraudulently sold the family house that was registered under her husband's name. Her husband had left several years earlier to reside in India, and Mrs. Dhillon used a special Power of Attorney that he had not signed. In contravention of a court order, none of the sale proceeds were given to Mr. Dhillon.

In the 2005 case of *Royal Bank v. Parmar et al*, Parmar signed her name to a mortgage on a house that a friend wanted to purchase in her name. The friend withdrew money in excess of the house's value. Parmar claimed that the bank had not done its due diligence to confirm the value of the house and that a bank employee had knowingly extended the mortgage beyond the house's value. The Court found that the bank owed no duty to Parmar to relate the borrowed money to the house's value. Parmar was liable for the mortgage.

In *Toronto Dominion Bank v. Jiang* (2003), Jiang dishonestly transferred property to himself and then obtained a \$200,000 mortgage from the TD Bank, all without the consent of the true owners. Upon

default, the Court ruled that the TD Bank was entitled to enforce the mortgage on the property. In *Vancouver City Savings Credit Union v. Hu* (2005), the fraud occurred when a solicitor did not pay out the primary mortgages on purchased properties. The mortgages were removed from title by forged documents. The BC Supreme Court found in favour of Vancouver City and restored the mortgages on title.

In other cases, the courts have found in favour of the innocent landowners. In *Rabi v. Rosu* (2006), unknown individuals posed as Rabi to transfer title of his condo to Rosu. A new \$247,860 mortgage was obtained through the TD Bank. The mortgage broker pocketed \$30,000 for assisting the transaction. The individuals who orchestrated the fraud disappeared with the money. Rabi only became aware of the fraud after receiving a City of Toronto tax bill in Rosu's name and, a short time later, a request from the mortgage company. Rabi successfully had the title of the condo restored to his name and the fraudulent mortgage set aside. The Ontario Supreme Court said a more prudent exercise of due diligence on the part of the bank, such as an in-person appraisal, may have prevented the fraud. The Court even ordered that the Bank pay Rabi legal costs of \$2,500.

In *Lawrence v. Maple Trust Company* (2007), Susan Lawrence's home was sold out from under her when an imposter forged her signature on a purchase agreement. To pay for this purchase, a mortgage was advanced by Maple Trust to a fake purchaser. On appeal, the Ontario Court of Appeal observed that Maple Trust chose to advance money and had some opportunity to avoid the fraud. The Court further noted that the law should encourage lenders to be vigilant when providing mortgages and places the burden of the fraud on the party that has the opportunity to avoid it rather than

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the innocent homeowner who played no role in the perpetration of the fraud.

In a Saskatchewan case, the CIBC sought to be reimbursed by the Registrar of Land Titles for money it advanced on a mortgage fraudulently obtained. The judge struck the mortgage off title (pursuant to section 68 of Saskatchewan's *Land Titles Act*) and CIBC lost its money.

So, what did the court decide in Ms. Zivic's case? The lenders claimed they were innocent victims of mortgage fraud and that they were dealing in good faith with a person who turned out to be a fraudster. They therefore argued that deferred indefeasibility should apply and that the mortgages should be enforced.

The Court focused on the timing of the transactions in this case. The fraudulent transfer of title occurred at the same time the funds were advanced. Registration of title and mortgage were simultaneous. Zivic was the registered owner when the lenders searched the title.

Bakiashvili was not yet the fraudulent owner of the property for which the funds were advanced by the banks.

The banks were dealing at

arm's length with someone who would only appear as registered owner once the funds were disbursed. The Ontario Supreme Court concluded that the lenders could not rely on deferred indefeasibility because they did not rely on the registry showing Bakiashvili as registered owner of the property.

Zivic was the more innocent party in this case because the lenders had the opportunity to perform due diligence and to better investigate the transaction with Bakiashvili. The Court said that the lenders *were* choosing to transact with the fraudsters. They used the same lawyer as Bakiashvili, which further compromised independent due diligence. The Judge invoked section 155 of the *Land Titles Act* that fraudulent titles are "void and of no effect." Judgment in *Home Trust Company v. Zivic* (2006) was therefore entered in favour of Ms. Zivic, the more innocent victim of identity theft.

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How the Fraud Is Facilitated

Several factors have made mortgage fraud easier to achieve. These include the depersonalization of the lending relationships and the automation of the buying and borrowing processes. Traditional long-term personal relationships between borrowers and lenders are lacking.

Mortgage lending has also become increasingly competitive — and inter-mediated — which increases the risk of identity fraud. Borrowers understandably squeeze lenders for fractions of interest rates and processing costs. In response, lenders streamline to reduce costs and speed up business. They turn to mortgage brokers and outsource mortgage administration. These practices present more opportunity for

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people to pass themselves off as someone else.

There is no standard due diligence conducted by banks to verify ownership. Appraisals are often done by averages, and even by computers. Mortgage fraud would mostly be prevented if someone from the bank or the appraisal company physically visited the home or personally made contact with the occupant. The sizzling real estate market, increased competition from mortgage vendors, the rush to make and close deals, and the growth of technology to both access personal information and produce fraudulent documents have all played a role.

Legislative Responses

Title and mortgage fraud are estimated to be a \$1.5 billion industry in Canada. Protracted litigation leading to conflicting *ad hoc* judicial decisions is not an adequate solution. Judges are left to reconcile apparently contradicting legislative provisions that were not enacted to deal with this modern problem. In a highly specific and unique set of facts, judges must decide who bears the loss resulting from a major fraud among several diverse innocent victims of the same crime.

Legislative reform and clarity as well as enhanced diligence, especially by those parties coming into direct contact with the fraudsters (such as witnesses to signatures, mortgage brokers, buyers, lenders, lawyers, and title registry officials), are necessary. Forgery, impersonation, and mortgage fraud are crimes under the federal *Criminal Code*, but these are difficult to prosecute because the perpetrators are often unknown or untraceable. Moreover, because the mortgage remains on title, as does the imposter's name, provincial legislation is necessary to reverse these fraudulent transactions and address the insurance and loss issues.

New legislation addressing real estate fraud varies by province. In the fall of 2006 the Ontario government introduced Bill 152 to protect landowners from this real estate fraud. It ensures that property ownership cannot be affected by registration of falsified mortgages, fraudulent sales, or counterfeit powers of attorney. Title will be restored to the rightful owner because any forged title document is deemed void. Safeguards will suspend and revoke accounts of known fraudsters so that they cannot register documents. Tougher rules for mortgage brokers are in place, and fines for real estate fraud-related offences increase from \$1,000 to \$50,000.

Ontario has created a Land Titles Assurance Fund to





compensate purchase and lending victims of mortgage fraud. Provincial driver's licences are more difficult to counterfeit so that false identification cannot be used for fraudulent deals.

Alberta has recently introduced several amendment bills which require better identification to register real estate documents. They also authorize the Real Estate

Council (an independent, non-government organization) to be more aggressive in investigations of mortgage fraud. The Registrar of Land Titles may refuse any transaction suspected of fraud. Criminal record checks are required for anyone licensed as a real estate agent, mortgage broker, or appraiser.

Registrars in Saskatchewan, Manitoba, and New Brunswick can also refuse to register a transfer or mortgage.

In addition to government action, many professional organizations and businesses across Canada, such as law societies, lenders, and real estate councils, are implementing guidelines to confront mortgage fraud.

How Can Property Owners Protect Themselves?

There seems to be little that property owners can do to specifically prevent or guard against title and mortgage fraud. However, everyone can generally protect themselves by guarding their identities and minimizing access to their personal information. One should not provide personal information over the Internet, over the telephone, or via the mail. In dealing with the more general problem of identify theft, the best course of action in preventing impersonation is to protect sensitive information such as credit card particulars.

When using the Internet, one should change passwords regularly and review business website privacy policies to ensure you are only working in a secure environment. Look for closed-lock symbols when entering sensitive data, install a secure firewall and anti-virus software, and clear the browser's cache after visiting several websites. One might also be careful about the personal identification one carries, such as a social insurance card, and one should shred documents that contain personal information before throwing them away or recycling them.

One should also be wary of suggestions of urgency or of cutting corners in any major transactions. A heightened sense of urgency on the other person's part may indicate fraud since fraudsters seek to complete the fraud quickly before they can be discovered. Such people may suggest that they do not have their verification evidence handy ("I just lost my wallet"), and this should also raise a red flag.

Feature Report on Real Estate Law

Where there are two or more clients involved in a single transaction, lenders should meet separately with each client and demand several forms of photo identification and check them thoroughly. If a registered owner is accompanied by an individual who is to benefit from a loan, the lender should consider meeting separately with the owner to be satisfied about his or her capacity and instructions.

One should also carefully review municipal annual property assessments and check monthly credit card, bank, and phone statements for any unauthorized use. Prior to completing loan or other credit applications, one should find out how the company disposes of them. And the periodical checking of credit ratings is a good idea too. All of these precautions may seem bothersome, but this is nothing in comparison to the effort, cost, and inconvenience of reclaiming one's property, identity, and good reputation.

What Is Next?

Dishonesty cannot be legislated away. New forms of fraud that exploit technology, personal information, system weaknesses, trust, and transactional efficiencies will continue to emerge, especially where the stakes are so high. Ultimately, we all pay for these fraudulent losses and we all have an interest in minimizing them.

There are many court cases about mortgage fraud in all provinces and the outcomes have been mixed, as have the resulting legislative reforms. There are innumerable ways in which such fraud can be committed, and sometimes family members have been the culprits. In such cases, it seems that the courts are more disposed to find the *innocent* family members more responsible for the fraud than third party lenders and buyers.

Some people have argued that identity and mortgage fraud should be separate, clearly-defined offences under the *Criminal Code* and that a national database of real estate fraud cases should be established. If mere possession of house-breaking instruments and

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stolen property are crimes from the old economy, perhaps it should now be illegal for someone to possess equipment for the manufacture of fake identification and other personal information, to use aliases, or to hold personal identification in more than one name.

The essence of the recent judicial decisions and legislative reform has been to shift the onus to third parties who have actual contact with the fraudsters to exercise more care and bear more risk. Professionals and lending institutions can utilize security teams and technology to prevent fraud and assist law enforcement when it occurs. Appraisers must be more demanding in requiring background checks and photo

Feature Report on Real Estate Law

identification. These are modest precautions in relation to the fraud that is possible.

Consumers can pressure financial institutions to tighten processes for authenticating client identification and other businesses to adhere to privacy legislation related to personal information. Homeowners can purchase title insurance to cover restoration of title and mortgage fraud.

It is too early to assess the impact that legislative and industry reforms will have on this crime or whether they will prevent the problems faced by Ms. Zivic and so many others. If such remedial measures prove fruitless, this new criminal activity may spur on the overhaul of the entire land registration and document-processing system in Canada.

Peter Bowal is a Professor of Law with the Haskayne School of Business, University of Calgary in Calgary, Alberta.

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