

# Insurance Issues: Risk Management

## Real estate fraud – a prevention primer

The Law Society recently issued an email alert to the profession on value fraud schemes, describing a typical scenario involving a fraudulent flip and other red flags of fraud. This edition of the *Insurance Issues: Risk Management* offers BC lawyers concrete practice tips to help recognize and manage the risk of unwittingly becoming a pawn in a real estate scam. Practical suggestions are offered for both value frauds and identity frauds.

### Value fraud – inflating the property price for a larger loan

A value fraud scheme typically involves a fraudster who agrees to purchase real property and flips it to a complicit purchaser at an artificially inflated price. This step positions the new purchaser to deceive a mortgage lender as to the true value of the property when obtaining a mortgage loan. While lending institutions make their own decisions to lend money on any particular matter, lawyers can play a role in fighting fraud.

#### Tips on fighting value fraud

##### **Make it a team effort**

Review the common characteristics of value fraud with your conveyancing staff. Direct them to advise you if they notice that a transaction has more than a couple of the characteristics.

##### **Consider asking for cancelled charges**

Instruct any staff conducting Land Title Office searches to order, if appropriate, searches that show all of the cancelled charges, not just the current charges. Such searches will disclose a rapid turnover of mortgages.

##### **Be cautious about flips**

Although “flips” are relatively common in the current active real estate market, be particularly careful whenever you encounter one. If the seller under the Contract of Purchase and Sale is not the same as the registered owner on title, ask your purchaser client questions to get a sense of whether

the transaction is legitimate.

##### **Copy picture ID**

Obtain and keep a photocopy of picture identification of buyers / borrowers to protect yourself from potential negligence claims. Simply recording the driver’s licence number is probably not sufficient protection. If you are receiving instructions from anyone other than the buyer / borrower, it is prudent to obtain a copy of that individual’s identification as well.

##### **Inform a lender client of a flip and obtain instructions**

When acting for a lender and the buyer / borrower in a “flip” situation, advise the lender that the transaction is a flip. Give the lender the amount of the purchase price under the original contract, and ask for further instructions.

##### **Consider consent to use of a power of attorney**

If a transaction involves the use of a power of attorney, consider obtaining the lender’s consent to accepting mortgage security signed pursuant to a power of attorney.

##### **Consider the payee**

If a large percentage of the mortgage proceeds are to be paid out to a borrower directly, or to parties other than the existing mortgagee or seller, make further inquiries.

Carefully review any directions you receive to determine if individuals or entities apparently unrelated to the transaction (other than a recognized

creditor) are to receive significant amounts from the mortgage proceeds. Is the lender aware of how the proceeds are being disbursed? Has it directed you to pay the money to third-party creditors?

##### **Insist on the evidence you need**

If presented with any circumstances that just do not pass the “smell test,” insist on the evidence required to put you at ease.

##### **Consider doing historical searches**

If suspicions are raised, consider doing historical searches to see if the property has been flipped at higher prices or mortgaged repeatedly.

### **Insurance Issues**

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*Additional subscriptions to this and the Law Society’s other regular publications may be ordered at a cost of \$50.00 per year, prorated at \$12.50 per quarter. [See the Benchers’ Bulletin for subscription information.]*

*If you have ideas on how to improve the Issues to make it more useful, please contact Susan Forbes, QC, Director of Insurance, Lawyers Insurance Fund.*

## Signs of value fraud

Here is a typical scenario involving a flip of property for fraudulent purposes:

- The fraudster enters into a legitimate contract to buy real property from an innocent seller at market value. The agreement includes the right of the buyer to assign the contract. The fraudster retains a lawyer to carry out the transaction.
- Almost immediately, the fraudster enters into a second contract with a nominee buyer (acting in concert with, or as a dupe of, the fraudster) at an inflated price.
- The nominee buyer takes the second contract to a lender to arrange mortgage financing.
- The lender approves a high-ratio mortgage on the inflated amount without independent valuation.
- The fraudster's lawyer is asked to act for both the lender and the nominee buyer.
- The lender is unaware of the first

(legitimate) contract and the fact that the lawyer is acting for the fraudster as well as the lender and the nominee buyer.

- The lawyer is asked to complete the transaction by preparing documents so that the property transfers directly from the innocent seller to the nominee buyer (the "assignee") at the lower price set out in the first contract.
- The lender advances mortgage funds in excess of the amount required to buy the property under the first contract and the lawyer is directed to pay the surplus to the fraudster or to someone apparently unconnected to the transaction.
- In addition to the warning signs described above, there are others:
- Often the nominee buyer signs a power of attorney in favour of the fraudster so that the nominee need not attend at the lawyer's office to sign documents.



- The nominee buyer appears to know or care little about the transaction and may be accompanied by a "handler" who understands the deal.
- The lawyer takes instructions from the fraudster, not the nominee buyer.
- A disbursement (often in the \$5,000 to \$7,000 range) is payable to the nominee or a seemingly unrelated party.
- Real estate commissions are rebated to the buyer or seller.
- The lawyer is paid higher than usual fees or even a bonus.

## Identity fraud — impersonating an owner

In an identity scam, the fraudster finds a property and poses as the owner. He or she then either secures mortgage financing from a lender or sells the property to an innocent third party. Once the mortgage funds or property proceeds are received, the rogue disappears.

The scams may be perpetrated by a person:

- using forged or fake documents:
- having a name that is identical to or "close enough" to that of the registered owner so that the identification appears legitimate; or
- convincing the lawyer to forego

the need for identification for some seemingly plausible reason ("I left my wallet in my sister's car" or "my wallet was stolen two days ago and I'm still waiting for my replacement ID").

In the competitive world of mortgage lending, the traditional adage of "know your client" unfortunately no longer holds true — and the lack of a relationship between the parties increases the risk of identity fraud. As borrowers shop from lender to lender for better deals and as those lenders streamline and speed up their business practices through mortgage brokers and by outsourcing mortgage administration, there are more

opportunities for a person to pass themselves off as someone else. To prevent being caught in a fraud and looked to as a possible source of recovery, lawyers must take their own steps to "know their clients" in the course of a conveyance or a mortgage financing.

### Tips on fighting identity fraud

#### Get picture ID

Insist on picture identification (unless you are certain of the client's identity through your own *personal* knowledge). If there is more than one client, insist that each produce separate photo identification. Avoid making accommodations requested by the client that result in variations to your

## Signs of identity fraud



In these scams, the lawyer does not know the borrower or seller personally. Some of the common characteristics may include:

- The borrower is not the registered owner of the property, but is relying on a power of attorney to borrow funds.
- Some discrepancy exists between the identification produced and the name of the owner as shown on title. The name on the identification produced may be close, but not identical to the registered owner's name, or

the name may be identical but the address or occupation differ.

- You are asked to contact the client exclusively by cell phone, or send documents or proceeds to the client at an address that is different than that on title or, if the borrower is a company, an address that is different than that shown on the corporate search.
- According to transfer documents that appear validly witnessed, the client recently used a different lawyer or notary to complete the purchase. For some reason, the client is now retaining you rather than simply returning to that lawyer or notary to complete this transaction.
- The client has a seemingly plausible and innocent explanation as to why she is unable to produce photo identification.
- The client is already known to you, but only as a client of another lawyer

in the firm. The client wants you to complete the deal on the basis that, although his identification is unavailable (again for some plausible reason), formal identification isn't necessary as you know him.

- The borrower has not placed fire insurance on the house, or asks you to obtain a waiver of the fire insurance requirement.
- The transaction must be completed in a hurry.
- Where property is jointly owned, two individuals attend, but only one has satisfactory identification. The other individual has some reasonable explanation for only having non-picture identification.
- One of the owners of a property held in joint tenancy comes to you alone, and asks you to sever the joint tenancy and place the mortgage against that owner's half interest.

standard procedure for checking identity.

### Keep a copy

Keep a photocopy of any picture identification that you take in the file, and ensure that it is legible. As noted, simply recording the driver's licence number is probably not sufficient.

### Obtain instructions if you have concerns

If you have any concerns, advise the lender to satisfy itself as to the borrower's identity and give you instructions to proceed or not.

### Watch for urgency

Be aware that there may be a heightened sense of urgency on the part of a fraudster, who wants to complete the fraud before it's discovered.

### Consider meeting separately with the registered owner

If the registered owner is accompanied by an individual who is to benefit from the loan, consider meeting separately with the registered owner to satisfy yourself as to that person's capacity and instructions.

### Provide only the assurances you can

Be careful as to the nature and extent of any assurances sought by the lender. Lawyers are increasingly being asked to go beyond the officer certifications contained in ss. 41 to 48 of the *Land Title Act*. Under those provisions, in taking someone's signature, you are not warranting that the individual is in fact the person named in the instrument. You are simply certifying that you believe that the person signing is

who they say they are.

### Take steps to protect against corporate identity fraud

If the borrower is a company, avoid the possibility of corporate identity fraud — the fraudster impersonating the authorized signatory of the company — through these further steps:

- Obtain your own updated copy of the corporate search. Do not rely on the client's old search;
- Follow the same steps with respect to obtaining picture identification for individuals signing on behalf of corporations that you would for individuals signing on their own behalf;
- In any solicitor's opinion you are

asked to provide, always include an assumption as to the genuineness of the signatures and material that you have relied upon, and a qualification of your opinion to that extent;

- Satisfy yourself that the individual signing on behalf of the corporation is authorized to do so, and that the requirements for executing a document on behalf of a company are met, particularly the requirement for multiple signing officers as provided in the by-laws of the company.

#### **Insist on the evidence you need**

As previously noted, if presented with any circumstances that do not pass the “smell test,” insist on the evidence required to put you at ease.

#### **What other steps can you take?**

##### **Land Title and Survey Authority**

If you suspect that title to a property or a charge is about to be dealt with fraudulently, consider registering the title with the Land Title and Survey Authority’s Activity Advisory Service. Once registered, an email will be sent to you within 20 minutes of any filing made with respect to the property.

Furthermore, consider contacting the

Registrar of the Land Title Office to discuss your concerns and whether other means might be available to protect against an unauthorized transfer or mortgage. It may also be appropriate to commence an action and file a caveat against the title to the property to prohibit any dealings with the property.

##### **Law Society**

If you still have reservations, contact the Law Society immediately. Law Society staff are experienced in these matters and can assist you in determining how to proceed to protect yourself and possibly help avert a fraud. They can also assist you if a report to law enforcement officials is warranted.

Lawyers are reminded of Chapter 4, Rule 6 of the *Professional Conduct Handbook*, which states that a lawyer must not engage in any activity the lawyer knows *or ought to know* assists in or encourages any dishonesty, crime or fraud.

##### **Title insurance**

If your client decides to buy title insurance, set out clearly what services you will — and will not — provide with respect to that policy. Failure to do so may result in the client holding you

responsible if, for example, the policy is never actually issued or coverage is denied because the title insurer’s procedures were not followed.

#### **More information on fraud**

BC real estate lawyers are encouraged to bring this risk management publication to the attention of their conveying staff. For more on the characteristics of fraudulent real estate schemes, see the Practice Tips column in the May-June, 2005 *Benchers’ Bulletin*: [www.lawsociety.bc.ca/publications\\_forms/bulletin/2005/BB\\_05-05-16\(Tips-fraud\).html](http://www.lawsociety.bc.ca/publications_forms/bulletin/2005/BB_05-05-16(Tips-fraud).html).

Fraudulent schemes have also become of great concern in Ontario, and the Law Society of Upper Canada has devoted significant resources to the investigation of complaints about lawyers being involved in these schemes. For more on real estate frauds and how law firms can detect and avoid them, see:

- Law Society of Upper Canada reference materials on fighting fraud: [www.lsuc.on.ca/news/a/hot\\_topics/fighting-real-estate-fraud-reference-materials](http://www.lsuc.on.ca/news/a/hot_topics/fighting-real-estate-fraud-reference-materials).
- A 2004 issue of *Law Pro Magazine*: [www.lawpro.ca/LawPRO/value\\_fraud.pdf](http://www.lawpro.ca/LawPRO/value_fraud.pdf).