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MORTGAGE AND REAL PROPERTY LAW REPORT

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REGISTRATION VALIDATES MORTGAGE PROCURED THROUGH FRAUDULENT POWER OF ATTORNEY

Can one defeat recovery of a secured loan obtained through fraudulent means? No, was the answer of the Ontario Court of Appeal in a recent decision which highlighted the importance of registration of security.

The case at hand was *Household Realty Corp Ltd. v. Liu* [2005] O.J. No. 5001. Mr. Liu and his wife, Ms. Chan, Hong Kong natives, immigrated to Canada and purchased a house as joint tenants. Mr. Liu's employment, however, kept him in Hong Kong for most of the time. During his absence, Ms. Chan developed a gambling habit and found herself deeply in debt. Unknown to Mr. Liu, Ms. Chan forged her husband's signature on a Power of Attorney and had it registered on title. Using the Power of Attorney Ms. Chan procured a $150,000.00 line of credit from TD Bank against the security of a mortgage registered against their home. Using the money from the line of credit, Ms. Chan paid $80,000.00 of her debts but continued to gamble.

By August, 2002, Ms. Chan's gambling debts amounted to $150,000.00. Using the fraudulently executed Power of Attorney once again, she secured yet another line of credit in the amount of $260,000.00 from CIBC with their house as collateral. Ms. Chan paid off and discharged the TD Bank line of credit from the CIBC mortgage funds. Despite the $260,000.00 line of credit from CIBC, Ms. Chan was unable to satisfy all of her debt. She then approached Household Realty Corp. Ltd. for a loan of $96,250.67, to be secured against their home as a second mortgage. Once again, the Household loan was procured using the fraudulent Power of Attorney.

In 2003, Ms. Chan defaulted on both the CIBC and the Household mortgages. Both mortgagees initiated proceedings against both Mr. Liu and Ms. Chan who counterclaimed against both mortgagees on the ground that the mortgages were void. Mr. Liu and Ms. Chan also sought injunctions restraining the mortgagees from selling their house.

At trial, the judge upheld the validity of both mortgages and concluded that the mortgages were valid upon registration despite the fact that they were obtained

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through fraudulent means. The basis of his decision rested on the policy underlying the Land Titles system of registration which upholds the validity of an instrument once registered in favour of a party that deals with the property in good faith for valuable consideration. In the instant case mortgagees had acquired an interest in the house by virtue of moneys advanced in good faith and without notice of the fraudulent Power of Attorney. That being said, mortgages once registered became effective and capable of being enforced by both mortgagees upon default by Mr. Liu and his wife, Ms. Chan.

"The fact that the power of attorney was fraudulently executed did not render the mortgages themselves fraudulent"

Liu appealed on the ground that the mortgagees, in failing to ascertain whether the Power of Attorney was duly executed, were negligent and could not, under the guise of registration of the mortgage security, recover what was obtained through fraudulent means. Dismissing the appeal of Mr. Liu and reiterating the finding of the trial judge, Justice Armstrong of the Appeal Court emphasized the importance of registered instruments under the system of Land Titles. According to him registration of the mortgages was the crucial component that determined their enforceability. The Power of Attorney was merely the means used by Ms. Chan to obtain the mortgage money. Both mortgagees had no knowledge of the fraudulent execution of the Power of Attorney and were therefore dealing *bona fide* without notice of the fraud.

The judgment serves to emphasize the paramountcy and importance of registration, especially where the parties dealing with the property have no notice of the fraud. This case serves to reinforce the policy behind the land titles system of registration which guarantees the accuracy of the property register and compensates innocent parties who suffer a loss as a result of any inaccuracy. It entitles *bona fide* parties for value and without notice of fraud to rely on the property register and the registrations on title.

Registration enforces the rights of such *bona fide* claimants. Ms. Chan could not benefit from her own fraudulent acts.

"TIME IS OF THE ESSENCE, ISN'T IT?"

A 1997 Hong Kong decision has been making waves across the ocean, in Canadian courts, and may have far-reaching effects on real estate lawyers and their clients.

In *Union Eagle Ltd. v. Golden Achievement Ltd.* [1997] A.C. 514 (Hong Kong P.C.), Union Eagle purchased a condominium unit from Golden Achievement for HK$4.2 million. Closing was set for September 30, 1991 on or before 5:00 p.m., and the agreement of purchase and sale had a standard clause stating that "time is of the essence".

Can you guess what's coming? Traffic! Before 5:00 p.m. on the closing date the purchaser's lawyer called the vendor's lawyer to say that his clerk was on the way with the closing package, but the clerk got stuck in traffic and arrived about 5:10 p.m. The vendor's lawyer, invoking the "time is of the essence" clause, took the position that the contract was terminated and kept the deposit. The purchaser sued.

At court there was no evidence that the vendor had been prejudiced by the lateness of the delivery, nor was the delay intentional. The vendor knew that the market was white-hot at the time, and that there was the potential for a big windfall if closing could be avoided somehow.

...the pendulum may be swinging back to a more technical interpretation... of contract terms like "time is of the essence".

The Hong Kong courts unanimously supported the vendor, at trial and on appeal, holding that where the contract states that "time is of the essence", as long as the vendor doesn't cause the delay, the purchaser bears the burden of its own delay, however great the burden or small the delay.

The vendor's decision (and the courts' decision!) was a lucrative one for the vendor because of a hyperactive Hong Kong condo market of the day: the vendor was able to turn around and sell the same unit for HK$19.5 million, an 800% gain over the original price!

What would a Canadian court today do in a fact situation like Union Eagle? Many commentators have stated that as a general rule, judges here would decide a case like Union Eagle in favour of the purchaser. Canadian judges, they argue, would reason that to overturn a deal honestly

entered into for a minor or technical breach, where the party seeking to get out of the deal was not prejudiced and is merely trying to get a better deal would go against modern doctrines of "good faith" and "fair dealing". Indeed, our judges and academics have been leaning that way in contract law.

But the pendulum may be swinging back to a more technical interpretation and application of contract terms like "time is of the essence". In *1473587 Ontario Inc. v. Jackson* [2005] O.J. No. 710 (Ont. S.C.J.), the contract between the parties specified that a deposit had to be paid within five days of signing, and there was a time is of the essence clause in the contract. Here the purchaser was a few days late in paying the deposit rather than a few minutes late, but as in Union Eagle the vendor was not prejudiced by the late payment of the deposit. The market was rising and another purchaser was waiting in the wings.

The court applied the rule in Union Eagle, concluding that the vendor was within its rights to terminate the contract, simply because the purchaser was late with the deposit, even though the lateness did not prejudice the vendor. There was no evidence of bad faith just because the existence of another purchaser may have influenced the vendor's decision to terminate. Moreover, vendors are not obliged to give notice immediately after a deadline in order to terminate, nor do they have to remind purchasers of their obligations. The appeal was dismissed in a short decision.

So is time always of the essence where the contract says so? It's likely too soon to say that the rule in Union Eagle is not the law in Canada, but decisions may be moving in that direction, and courts deciding these sorts of cases won't be able to ignore the Union Eagle reasoning.

EXECUTION ACT (ONTARIO) UPDATE - NEW EXEMPTION LIMITS

The value of goods exempt from seizure under the *Ontario Execution Act* has been increased to reflect inflation over time. Creditors should keep these limits in mind when making collection and recovery decisions. The new values exempt from seizure by a judgment creditor effective December 14, 2005 are as follows:

Clothing	$ 5,650.00
Furniture	11,300.00
Tools of Trade	11,300.00
Farm Equipment	28,300.00
Automobile	5,650.00

NO SPECIAL DUTY TO WARN OWED BY FINANCIAL INSTITUTIONS TO INVESTORS

Banks Not Providing Financial Advice

The Ontario Superior Court of Justice recently dismissed a claim by a group of investors against several financial institutions on the grounds that there was no duty to warn the borrowers of specific risks associated with loans for mutual fund investments which included margin call features.

The plaintiffs borrowed money for leveraged investments in mutual funds and incurred losses when the values of the funds declined. The plaintiffs invested money through a financial advisor who established a program whereby his clients could borrow funds from a financial institution for the investments. The advisor would provide his client with the documents required by the financial institution and the financial institution would then approve the application, or not, and fix it for a certain amount. The loan funds would then be advanced to the financial advisor for investment in the mutual funds. The group of investors as plaintiffs alleged that a fiduciary relationship was established and a subsequent duty was owed by the financial institutions to the plaintiffs.

The matter reported as *Baldwin v. Daubney* [2005] O.J. No. 5330 was heard on a motion for summary judgment brought by the financial institutions to dismiss the plaintiffs' claims on the ground that there was no triable issue.

In dismissing the claims and granting summary judgment, Mr. Justice Spence found that "the financial institutions did not owe a duty of care to the plaintiffs to advise them about the risks of investing their loans in mutual funds."

The banks and trust companies did not communicate with the plaintiffs or give the plaintiffs any reason to rely on them and were not acting as agents for the borrowers. The fact that the financial advisors submitted loan documents directly to the financial institutions did not imply that the advisors were acting on behalf of the banks. The banks had no special duty to warn of the risks associated with the particular investments.

Mr. Justice Spence was of the view that there was no special duty established and no new duty of care to advise with respect to these loans. The banks were lending money, not providing financial advice.

PLANNING AND DEVELOPMENT NEWS CORNER

Provincial Development Facilitator for Ontario

In August 2005 the Office of the Provincial Development Facilitator for Ontario was established. It operates almost as a development ombudsman and its job is to help municipalities, developers and community groups to resolve disputes over land growth, land planning issues, infrastructure and environmental protection issues. It is arm's length to the government and is available to private citizens as well as the parties set out above. It is likely that its focus will be to try and resolve disputes before they end up being referred to the Ontario Municipal Board. The office is intended to be a resource, primarily acting as a mediator but its decisions are not binding. Time will tell whether parties utilize this resource or it becomes redundant.

Bill 51: Planning and Conservation Land Statue Law Amendment Act (Ontario)

Draft planning legislation has been introduced at Queen's Park.

This bill is intended to reduce the power of the Ontario Municipal Board (OMB) which is perceived as development friendly, and it will cause significant changes in the way the development industry operates. It has passed first reading but industry groups are hoping for significant amendments.

In particular developers should note that this act prevents a developer from filing an application to amend the official plan changing the designation of an employment area to any other use. The only time that the designation can be challenged is every five years when the municipality must up-date its official plan. Moreover, the act provides that when a matter is referred to at the OMB that only information, reports, etc., provided at the time the matter was heard at the municipal council may be introduced. That means even with a positive planning report from a municipality, you will be forced to make a presentation and introduce into evidence all of your consultants reports, etc. As one industry commentator stated, you will have to prepare for council as you would prepare for the OMB and this means much more time, advanced planning, consultants reports and expense.

NEW LAWYERS

We are pleased to announce the additions of Bryan Whealen and Cheryl D'Souza to our Firm.

Bryan Whealen

Bryan Whealen recently returned to our firm after working as in-house counsel with a registered education savings plan dealer. Bryan graduated from the University of Windsor Law School in 1980 after obtaining an undergraduate degree in History. He was called to the Ontario Bar in 1982. His work experience includes a role with the Federal Government in Ottawa as Special Assistant to the Parliamentary Secretary to the Minister of Justice and Attorney General of Canada, as well as in-house counsel to Mortgage Lenders in Toronto. His practice consists of mortgage and debt enforcement.

Cheryl D'Souza

Cheryl D'Souza was educated in India and graduated at the University of Mumbai (Bombay) and was called to the Bar in India in 1990. She practised as a civil litigator in the Supreme Court of India and in the Indian Regional High Courts. She immigrated to Canada in 1999 and completed her Canadian legal education at the University of Toronto and was called to the Ontario Bar in 2005. Her practice areas include commercial real estate, with particular emphasis on land development, condominium law and commercial financing as well as general corporate /commercial matters.

Baker Schneider Ruggiero LLP is engaged in various areas of law with particular emphasis on the following:

- Commercial Lending
- Subdivision and Condominium Development
- Mortgage Enforcement (Commercial and Residential)
- Debt Restructuring
- Real Property Litigation
- Commercial Litigation
- Corporate/Commercial/Leasing