CHAPTER 5

THE PROFESSIONAL LIABILITY OF MORTGAGE BROKERS

Learning Objectives

After studying this chapter, a student should be able to:

- ☑ List the elements of negligence and negligent or fraudulent misrepresentation and describe how they might arise in a mortgage broker's daily activities
- ☑ Discuss the principle of vicarious liability and its significance to mortgage brokers
- ☑ List the *Criminal Code* elements applicable to mortgage fraud and explain the differences between identity fraud and value fraud
- ☑ List the indicators of a potential identity fraud and value fraud transaction, and provide examples of fraud prevention techniques
- ☑ Discuss the various provisions of the *Competition Act* that might apply to a mortgage broker's practice
- ☑ Describe how fiduciary and agency relationships are created
- ☑ Explain the duties a fiduciary owes to their beneficiary and be able to apply them to a mortgage brokerage relationship
- ☑ Discuss the money-laundering process and what role mortgage brokers can play in the fight against money-laundering

INTRODUCTION

Mortgage brokers, like any other professionals, expose themselves to the risk of liability when acting in the course of their practice. The courts of British Columbia require high standards of conduct from mortgage brokers acting in their professional dealings; this standard of care is not one of perfection, but it can sometimes be very close to it. You should be aware that the courts have little sympathy for mortgage brokers, whom they treat as professionals, and insist upon high standards of conduct being met.

NEGLIGENCE

The tort of negligence involves a failure by a person to exercise a duty of care in circumstances which require that person to take care. The potential scope of negligence is very great because the number of situations in which the law may determine that a duty to take care exists is unlimited; however, not every accident will support a claim of negligence. Before a person will be held to be negligent, certain criteria must be met. The plaintiff must prove three things:

1. **That the Defendant Owed the Plaintiff a Duty to Take Care.** A person will be held to owe a duty to take care to all persons whom they can or should reasonably foresee as being affected by their actions. In addition to situations where foreseeability of harm exists, the courts in Canada are willing to find a duty of care in situations where, as a matter of policy, it is felt the public has a right to expect persons involved in a particular activity to take care in the way they conduct themselves in that activity.
2. **That the Defendant Breached the Standard of Care Owed.** The relevant standard of care in any situation of duty will be to take the same care that a reasonable person would take in all the circumstances of the case. Generally, the greater the risk involved in a particular activity, the higher the standard of care that will be imposed on persons engaging in that activity. For mortgage brokers, the standard of care that must be met is that of a reasonably prudent mortgage broker. Mortgage brokers will not simply be held to the same standard as a "regular person". A court may hear evidence from an experienced mortgage broker when determining whether or not the required standard of care was met in a particular case.
3. **That the Damages Suffered by the Plaintiff as a Result of the Defendant's Breach Were Not Too Remote in Law.** The type of damage caused must have reasonably been within the contemplation of the defendant as a possible consequence of their acts or omissions. Types of damage not reasonably foreseeable are considered too "remote" in law, and a plaintiff will not be able to get compensation for them.

Where a plaintiff is able to prove that the defendant owed them a duty of care which the defendant failed to fulfil, and that the failure of duty resulted in reasonably foreseeable damages, the plaintiff will succeed with a claim in negligence. If any one of the required elements is not proven by the plaintiff, the action in negligence will fail.

Example

A man ran for a train that was starting to leave the train station. Two railway employees tried to help him get on board the moving train and in the process dislodged the man's package. The innocuous-looking package turned out to contain fireworks, and when it fell on the tracks it exploded. The vibrations from the explosion knocked down some scales at the opposite end of the train platform which fell on a woman and injured her. She sued the railway company in negligence but failed to prove her claim. The Court held that there was no duty of care owed to the woman by the railway employees concerning the package. There was no way the railway employees could have reasonably foreseen that the package would explode and harm the woman; therefore, there was no duty owed to the woman as a person likely to be affected by their actions. In the absence of a duty to take care, the dropping of the package did not amount to negligence toward the woman.

How Does Negligence Affect Mortgage Brokers?

The law imposes a duty of care on the part of a mortgage broker to maintain a reasonable standard of conduct in the performance of their professional tasks. When a mortgage broker fails to perform to the required standard of care and damage or loss results to a party, the mortgage broker can be found liable.

The cases described below illustrate the importance of mortgage brokers exercising a reasonable degree of care when carrying out their business by, among other things, relaying accurate information to clients, performing reasonable due diligence, as well as properly accounting for, and advising their clients on, the risks associated with any transaction that they are involved in.

Normak Investments Ltd. v. Belciug, 2015 BCSC 700

In the case of *Normak Investments Ltd. v. Belciug*, a mortgage broker was found negligent for passing false information from a borrower or a third party to a lender without first taking steps to verify it. In that case, the mortgage broker submitted a mortgage loan application and a Form 9 disclosure statement to the lender, in support of a borrower's application for a second mortgage. In these documents, the mortgage broker indicated that the property had a value of $451,000 and that there was a first mortgage on the property with a balance of $218,000. The mortgage broker also provided information about the borrower's employment, income, and assets to the lender. The mortgage broker signed the declaration at the bottom of the Form 9 disclosure statement stating, "I have fully completed the above Investor/Lender Disclosure Statement in accordance with the *Mortgage Brokers Act* (the "MBA") and regulations and declare it to be accurate in every respect." On the strength of this information, the lender loaned $70,000 to the borrower in exchange for a second mortgage on the property.

As it turned out, the actual balance of the first mortgage was approximately $396,000, not $218,000. A third party (who was not the borrower) had given the mortgage broker a fraudulent mortgage statement that understated the balance of the first mortgage. The mortgage broker did nothing to verify the accuracy of the statement he received from the third party. Additionally, the employment, income, and asset information passed on by the mortgage broker to the lender were false. Again, the mortgage broker had unwittingly received false information about these matters from the borrower or a third party that he then passed on to the lender without verifying it.

The borrower defaulted on their mortgage payments and the property was sold for net proceeds of $392,000, which was not even enough to repay the first mortgage. Accordingly, the lender lost its entire investment and sued the mortgage broker in negligence. The Court found that the mortgage broker had acted negligently and ordered the mortgage broker to pay compensation to the lender. The Court stated:

> [The mortgage broker's] conduct on this occasion falls considerably short of the standard of care a reasonably prudent mortgage broker would exercise in the circumstances. No mortgage broker can guarantee an investor the accuracy of every statement or piece of information supplied to them in considering a particular investment. What is required is the exercise of reasonable care. Taking into account the importance of the information, the purpose for which the statement was made, the foreseeable use of the statement, the probable damage that would result from an inaccurate statement, and [the mortgage broker's] professional status, I have no difficulty finding that [the mortgage broker] was negligent. He never met with [the borrower]. He obtained information about her employment, assets and creditworthiness. He may have obtained that information from a third party. Regardless of its source, he made no effort to verify its accuracy. He obtained the MCAP mortgage statement from a third party. He did not disclose this to the plaintiff and made no efforts to verify the accuracy of that statement. Having failed to do so, he then supplied all this information to Dewshi [the lender's representative], declaring it to be accurate. […] He was under a duty to use reasonable care to ensure that the representations he made and the information he supplied were accurate. He did not do so.

ALERT

Apart from being sued in civil court, mortgage brokers can also be disciplined by BC Financial Services Authority (BCFSA) if they pass information from borrowers on to lenders without first verifying the information. BCFSA states:

> Mortgage brokers cannot say that it is not their responsibility to verify the information being given to them during the application process. Lenders indicate they assume that mortgage brokers have verified the information before forwarding it on. This office takes the position that a mortgage broker has a duty to ensure the information being sent to a lender has been verified. […] reasonable due diligence must be undertaken to ensure that the information being passed on to lenders is accurate. [...] If mortgage brokers do not verify the information they are forwarding to lenders, then mortgage brokers should advise the lenders in writing that none of the information has been verified.[1]

In *Asadi (Re),*[2] a submortgage broker's registration was canceled for life and the submortgage broker was required to pay an administrative penalty of $15,000 and partial investigation costs of $8,000. Several inconsistencies were discovered in mortgage applications submitted by the submortgage broker to various lenders. Considering the evidence, the Registrar of Mortgage Brokers determined that the submortgage broker had breached the MBA by failing to conduct appropriate due diligence and "know your client" procedures, among other things. For example:

- In one application, the borrower's stated employer (a healthcare organization) was not registered in the corporate registry and did not match the name of the borrower's last known employer in their credit report. A few months later, the submortgage broker submitted a second mortgage application for this borrower that contained inconsistent information about the borrower's income and assets than the first application. Included in the second application was a bank statement for the borrower which showed net pay deposits that were far less than the borrower's stated income, and the income shown in the borrower's tax documents.
- In another application submitted by the submortgage broker, the borrower claimed to own a fleet of taxi cabs. However, when the registrar contacted the cab company, they were advised that the borrower was only a driver, not an owner, and that he had quit in order to become an electrician instead.

As a mortgage broker, taking reasonable care in your business activities will help to avoid BCFSA sanctions, negligence lawsuits, and damage to your professional reputation. This includes taking reasonable steps to verify information before passing it on to lenders. Information that may need to be verified could include:

- Suspicious or unusual employment or income documents (e.g., job letters that contain spelling errors or come from organizations that cannot be found in the corporate registry or through internet searches, tax documents that do not support what the borrower says their income is, bank deposits that do not support the borrower's income in their tax return)
- Suspicious or unusual down payment sources (e.g., an 18-year-old student claiming to have hundreds of thousands of dollars of down payments as a result of "savings")
- Suspicious or unusual asset and debt profiles (e.g., a recently divorced client who said that they received a small divorce settlement appears to own multiple properties in British Columbia)
- Purchase prices or appraisals that do not accord with the area and type of property
- Suspicious or unusual occupancy declarations (e.g., the person is claiming that the property will be owner-occupied in the mortgage application, but the property is much farther from their office than their current home)
- Suspicious or unusual loan balances in mortgage statements (e.g., a mortgage was registered on title a few months ago to secure a loan of $1,250,000, but a current mortgage statement supplied by the borrower shows that the current loan balance is only $500,000. Further, no reasonable explanation is given for the significantly reduced balance)

- Information that comes from third parties as opposed to from the borrower directly

Mortgage brokers should examine all components of a loan application critically, in context, to spot unusual, incomplete, inconsistent, or incorrect information.

Royce Holdings Inc. v. Jupe, 2018 BCSC 2025

The "reasonable care" standard as described by the Court in the *Normak Investments* case was later applied in the case of *Royce Holdings v. Jupe*. In that case, a submortgage broker had acted for a lender with respect to two transactions occurring at different times but involving the same borrower and in relation to the same property. The two mortgage investments made by the lender were secured by a second mortgage against the property. Ultimately, the property was sold in foreclosure proceedings (commenced by the first mortgagee) for an amount that was less than the balance of the first mortgage. As a result, the lender lost its entire investment and sued the submortgage broker (among others), alleging that the submortgage broker had acted negligently.

The Court looked at the circumstances surrounding each of the two investments separately and considered the submortgage broker's actions in each situation. With respect to the first investment, the Court found that the submortgage broker had acted reasonably in basing his advice to the lender upon an appraisal by an independent and qualified appraiser, a mortgage statement for the first mortgage registered against the property, and the borrower's credit report and debt-repayment history. The Court determined that there was nothing inaccurate about the information that the submortgage broker had provided to the lender in support of the first investment and that he had acted honestly and applied his knowledge and experience to the best of his ability in the circumstances.

The facts surrounding the second investment, however, were quite different. When advising the lender with respect to the viability of second investment, the submortgage broker represented to the lender that the appraised value of the property had increased since the first investment. He did so despite the fact that he did not actually have an updated appraisal of the property, and knowing that real estate values were dropping in the area. The submortgage broker also failed to properly consider the increased risk associated with the second investment or advise the lender with respect to this increased risk. The Court held that had the submortgage broker completed the appropriate due diligence and fully explained the increased risks, the lender would not have made the second investment. As a result of all of the foregoing, the submortgage broker was found to have acted negligently in relation to the second investment and was ordered to pay the value of the second investment to the lender.

Vicarious Liability

A mortgage brokerage will be held liable for the negligent or other wrongful acts of its submortgage brokers when those acts are committed in the ordinary course of employment. This common law principle is known as vicarious liability.

Where an employee commits a wrongful act in the ordinary course of employment, the injured party can sue both the employee and the employer for damages caused by the employee's act. For example, in each of the *Normak Investments* and *Royce Holdings* cases discussed previously, the negligent broker's employer was held to be vicariously liable for the broker's conduct. However, if the wrongful act does not occur in the ordinary course of employment, the employer will not be liable.

> ### *Example*
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> An employee of a dairy used the dairy's truck to take his family to the movies outside of work. While using his employer's truck, the employee caused a collision. The Court found no vicarious liability on the facts because the employee's wrongful act did not occur in the course of performing his employment duties. The employee alone was found liable to the plaintiff.

Employers may even be vicariously liable for wrongs such as fraud or assault, if such acts are committed in the course of an employee's employment. It is important to note that submortgage brokers are treated by the courts as employees. For this reason, it is important for designated individuals to properly supervise their brokerage's submortgage brokers in the course of their business, and for submortgage brokers to keep their designated individuals fully apprised of their business activities.

MISREPRESENTATIONS AND DECEIT

Misrepresentation can be defined as any manifestation by words or other conduct by any one person to another that, under the circumstances, amounts to an assertion not in accordance with the facts. Generally speaking, mortgage brokers may face liability for two types of misrepresentation:

1. negligent misrepresentation; and
2. deceit and fraudulent misrepresentation.

misrepresentation
a false statement of fact which is relied upon by another person to their detriment

Negligent Misrepresentation

Negligent misrepresentation is also referred to as negligent misstatement. The principles governing liability in negligence also apply to negligent misrepresentation. The Supreme Court of Canada has stated the particular requirements for liability for negligent misrepresentation as follows:

1. there must be an untrue statement;
2. it must have been made negligently;
3. there must be a special relationship between plaintiff and defendant giving rise to a duty of care; and
4. there must be reasonable reliance by the plaintiff on the negligent statement.

Where the reliance results in foreseeable loss, the person who relied upon the statement may recover damages from the person who made the negligent misrepresentation.

The special relationship giving rise to a duty to take care will be created where a skilled person, or expert, gives advice in the course of their business to a person who is reasonably going to rely on that advice. In such a situation, there are three courses of action open to the skilled person:

1. the skilled person can refuse to give the advice or opinion sought;
2. the skilled person can give the advice or opinion with a clear qualification that they accept no responsibility for the accuracy or

reliability of the advice; or

3. the skilled person may give the advice with no qualification or disclaimer of liability.

If a skilled person chooses option (3), then that person must take reasonable care in giving that advice or face liability for losses arising from the advice if it is negligently given.

Liability for negligent misrepresentation can be imposed on mortgage brokers, who are considered by the courts as skilled persons or experts in the area of mortgages. This means that where a mortgage broker is asked for advice or an opinion in a business relationship, the mortgage broker must be aware that if they elect to give advice or state an opinion without qualification, the mortgage broker faces the risk of liability should the advice or opinion be negligent.

As a Mortgage Broker...

It is important to act carefully when making representations in the course of business. Failure to do so can lead to liability for negligent misrepresentation.

For example, in *Pryce v. Vuckovich*,[3] an Ontario mortgage broker, who was also a professional accountant, had been providing mortgage broker services to a family of private lender/investors for several years. Two sisters in the family inherited a sum of money from their mother and the mortgage broker offered the sisters various mortgage investment opportunities, which they invested in. Neither sister had any prior experience as mortgage lenders/investors. They trusted the mortgage broker to guide them appropriately.

The events which led to the lawsuit were as follows. The mortgage broker received a call from another mortgage broker whose borrower clients required a second mortgage, urgently. The borrower's broker told the mortgage broker that there was an appraisal on the property but that she did not have time to send it over to the mortgage broker. The borrower's broker indicated that the appraised value of the property was $3,690,000. The borrower's broker asked whether the mortgage broker had any lender clients who might be interested in the opportunity.

The mortgage broker contacted the sisters and recommended the mortgage investment opportunity to them. The mortgage broker told the sisters that there was a $3,690,000 appraisal of the property and a first mortgage of $1,900,000. The mortgage broker did not warn the sisters that it was risky to rely on the appraised value of $3,690,000 because the mortgage broker had not actually seen a copy of the appraisal.

Based on the mortgage broker's recommendation, the sisters chose to loan $600,000 on a second mortgage. The mortgage soon fell into default and the property was sold for only $960,000, far less than the alleged appraisal value. As it turned out, there were significant problems with the appraisal which the mortgage broker only discovered later, after the fact, when she eventually obtained a copy. The net sale proceeds were applied against the first mortgage only and there was nothing left to repay the sisters. The sisters lost their entire $600,000 investment and sued the mortgage broker for negligence. The Court found that the mortgage broker's recommendation of the mortgage investment opportunity, without ever having reviewed the appraisal, amounted to negligent misrepresentation. The Court stated:

> There is no question that [the mortgage broker] acted negligently here. She recommended the …mortgage to the Pryce family without her ever seeing an appraisal of the property…[the borrower's broker's] excuse for not faxing the appraisal to [the mortgage broker] makes little sense…there was no genuine reason why [the mortgage broker] had to rely on verbal confirmation of the appraisal without her own personal review of the document.

The mortgage broker was held personally liable for the sisters' loss and ordered to compensate them for her negligent misrepresentation. This case, as well as the *Normak Investments* and *Asadi(re)* cases discussed previously, highlight the importance of verifying information (including information from a borrower, a borrower's representative, or another mortgage broker) before passing it on to a lender.

Deceit and Fraudulent Misrepresentation

The tort of deceit is similar to the concept of fraudulent misrepresentation which applies to the law of contract. *Deceit* and fraudulent misrepresentation are different from negligent misrepresentation in two respects. First, they involve a sense of moral fraud as opposed to carelessness. The person making the statement intended to deceive the other person when making the representation. Second, a person does not need to be an expert to be liable. When a misrepresentation is false and is made either knowingly (without a belief in its truth) or recklessly (not caring whether it is true or false), the person making the misrepresentation is liable for damages in tort, in addition to any further right the party may be able to exercise under contract law.

deceit
a fraudulent or deceptive misrepresentation used by one person to deceive or trick another person ignorant of the true facts

ALERT

As explained in Chapter 2: "The *Mortgage Brokers Act* and Professional Ethics", there have been instances of registered mortgage brokers improperly facilitating the mortgage brokering activity of unregistered persons (i.e., "fronting"). In one case, an unregistered person would find borrowers, meet with them, help them prepare mortgage applications, and then have a registered person submit the mortgage application to lenders. The registered and unregistered person would then share the commission payable for the mortgage transaction.

Fronted loan applications can create risk for borrowers and lenders because they may include falsified documents or information that is used to mislead lenders and inflate an applicant's borrowing capacity. BCFSA has taken disciplinary steps against several registered mortgage brokers who have fronted for unregistered persons. In addition, if a borrower or lender experiences harm as a result of a fronted loan application, the fronting mortgage broker may be held liable for negligent or fraudulent misrepresentation and may also be required to pay damages.

For these reasons, it goes without saying that mortgage brokers must never knowingly participate in fronting. It may also be prudent for mortgage brokers to perform additional due diligence and review mortgage applications that originate from external sources, to avoid unwittingly becoming involved in fronting.

ERRORS IN DRAFTING AGREEMENTS

A mortgage broker must understand the basics of contract law, including the principles relating to offer and acceptance, counter-offers and revocation of offers. Liability can often arise if these basic principles are not observed. The message from the courts is clear: know basic contract law – if you have any doubts, seek legal advice. Contract law is dealt with in detail later in this manual.

On occasion, a mortgage broker may be required to provide legally enforceable clauses or documents which reflect the intent of the parties. These documents should be drafted in simple, accurate and understandable terms. Jargon, abbreviations, colloquialisms and any terms or phrases, which give rise to uncertainty, should be avoided. When in doubt, all parties should be referred to an appropriate legal advisor.

BREACH OF FIDUCIARY DUTY

In some circumstances, a mortgage broker may enter into a special legal relationship with another person, known as a fiduciary relationship. When this occurs, the mortgage broker becomes a *fiduciary,* and will be required to adhere to certain fiduciary duties such as the duty of loyalty, the duty to avoid conflicts of interest, the duty of full disclosure, and the duty of confidentiality. Breaching one's fiduciary duties is a serious matter and can result in significant legal liability for the fiduciary. The law of fiduciaries will be discussed in more detail later in this chapter.

fiduciary
a person who holds a position of trust with respect to someone else and is obliged, by virtue of the relationship of trust, to act solely for the other person's benefit

STATUTORY AND INDUSTRY LIABILITY

In addition to being found liable by the courts, a mortgage broker can be investigated and disciplined by the Registrar of Mortgage Brokers. This is known as statutory or regulatory liability. The Registrar's functions and powers are set out under the MBA and have been discussed in a previous chapter.

A mortgage broker may also face disciplinary proceedings by a professional association of which the mortgage broker is a member, known as industry liability. Generally, an association will be incorporated as a society under the *Societies Act* and have its own constitution and by-laws, as well as a code of ethics and/or agreed standards of business practice. Professional associations can take jurisdiction over their members to deal with complaints that a mortgage broker has breached the code of ethics or has otherwise conducted themselves improperly. The penalties which are available to professional associations depend upon their constitutions and bylaws, and range from a reprimand to a suspension or expulsion from membership. Sometimes, a member can be ordered to pay the costs of the hearing in the event that a penalty is assessed.

The disciplinary committee of a professional association does not have the power to suspend the mortgage broker's registration; however, the suspension or expulsion from membership may deny the member from access to association services and have obvious detrimental consequences in terms of a mortgage broker's reputation in the industry.

WHAT IS THE BOTTOM LINE?

The law is imposing increasingly strict standards on all professionals, including mortgage brokers. Because the law is constantly changing and developing, accepted practices of the mortgage industry will also change. It is imperative that you keep abreast of these changes. It may not be a good defence for mortgage brokers to maintain that they conducted themselves in accordance with the accepted practice at the time. The customs of the industry as a whole are evolving to meet the stricter requirements of the law, which in turn reflects a heightened sensitivity to the protection of consumers.

All mortgage brokers must consider taking the time to learn how to recognize situations which put them at risk of liability and how to avoid these situations.

MORTGAGE FRAUD

The incidence of mortgage fraud is increasing dramatically in Canada and has cost lenders and insurers millions of dollars. Since statistics in Canada have not been consistently monitored over time, most statistical data originates from the United States. People are buying, selling and investing in real estate at unprecedented rates, which unfortunately has resulted in increased opportunity for fraud. As a result, it is important that all the parties involved in mortgage transactions, from mortgage brokers, lenders, and real estate lawyers, to consumers, be aware of what mortgage fraud is, who is injured by it, and learn what can be done to detect and prevent it. Mortgage brokers have a professional responsibility to be aware of the different types of mortgage fraud that are occurring today, along with the responsibility to identify circumstances that may be fraudulent. This section will introduce the crime of mortgage fraud to you and will also describe various methods of due diligence techniques and red flags to look out for.

Mortgage Fraud: A Crime

Mortgage fraud is a criminal offence in Canada. The fraudster can be found guilty of fraud as per section 380(1) of the *Criminal Code*, and can also be found guilty of theft of stolen funds under section 334 of the *Criminal Code* (R.S. 1985, c. C-46):

> 380. (1) Every one who, by deceit, falsehood or other fraudulent means, whether or not it is a false pretence within the meaning of this Act, defrauds the public or any person, whether ascertained or not, of any property, money or valuable security or any service,
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> (a) is guilty of an indictable offence and liable to a term of imprisonment not exceeding fourteen years, where the subject-matter of the offence is a testamentary instrument or the value of the subject-matter of the offence exceeds five thousand dollars; or
>
> (b) is guilty
>
> (i) of an indictable offence and is liable to imprisonment for a term not exceeding two years, or
>
> (ii) of an offence punishable on summary conviction,
>
> where the value of the subject-matter of the offence does not exceed five thousand dollars.
>
> 334. Except where otherwise provided by law, every one who commits theft
>
> (a) if the property stolen is a testamentary instrument or the value of what is stolen is more than $5,000, is guilty of

(i) an indictable offence and is liable to imprisonment for a term of not more than ten years, or

(ii) an offence punishable on summary conviction; or

(b) if the value of what is stolen is not more than $5,000, is guilty

(i) of an indictable offence and is liable to imprisonment for a term not exceeding two years, or

(ii) of an offence punishable on summary conviction.

In addition, the *Criminal Code* contains various prohibitions against theft or fraud related specifically to mortgage transactions. For example:

- section 331 makes it an offence for a person who acts under a power of attorney for the mortgage of property to fraudulently use the proceeds of a mortgage loan for an unauthorized purpose;
- section 385 makes it an indictable offence for a seller or mortgagor (or his or her agent) to fraudulently conceal certain title information, including mortgage information, to induce a buyer or lender to accept the title offered; and
- section 387 makes it an offence for a person who knows about an unregistered mortgage to fraudulently sell the property. The section does not define the word "fraudulently" nor specify in what circumstances the sale of a property with an unregistered mortgage would violate this provision.

Mortgage Fraud Defined

Black's Law Dictionary defines fraud as:

> A false representation of fact, whether by words or by conduct, by false or misleading allegations, or by concealment of that which should have been disclosed, which deceives and is intended to deceive another so that he shall act upon it to his legal injury.

Mortgage fraud occurs when a fraudster intentionally provides false or misleading information in order to obtain a mortgage on a certain property. Mortgage Professionals Canada has defined mortgage fraud as:

> The material misstatement, misrepresentation or omission relied upon by an underwriter or lender to fund, purchase or insure a mortgage loan.

There are a number of factors that have led to the increase in mortgage fraud across North America. While considerable improvements in internet and computer technology have made the organization and processing of mortgages more efficient by using computerized registry systems, this advancement in technology has also made it easier for criminals and fraudsters to access information in order to commit mortgage fraud. Because of the numerous parties involved in a mortgage transaction (mortgage brokers, real estate agents, lawyers, lenders and consumers) many of the players never meet directly, especially when most of the work can be completed electronically.

Advancements in technology are also responsible for the anonymity that has entered into the home buying process. Home buyers no longer have to meet face-to-face with lenders; appraisals can be done by computers (such as the Automated Valuation Models); and funds can be transferred electronically. Anonymity has allowed more mortgage criminals to creep in without detection.

With the increased ease and efficiency of the mortgage process has come an increase in demand for mortgages and mortgage providers. This increase in demand has spurred a heightened level of competition amongst mortgage providers, who have found themselves having to create incentives to distinguish themselves from the rest. Such a variety of options available to consumers means that it is more difficult for regulatory bodies to monitor all actions. Consequently, barriers to money lending have decreased. If a person can not obtain a mortgage with one lender, there are many other options available now that will expedite the process.

Finally, with the high frequency of mortgages being secured these days, naturally comes the rush to close deals quickly. This can result in a lack of the performance of appropriate due diligence that is normally necessary due to increased time pressures. With lower standards of due diligence comes an inherent vulnerability to criminal activity. The less a process is monitored, the more attractive and accessible it is to commit fraudulent activities.

The victims of mortgage fraud are numerous, as they potentially involve all of the players in the transaction including lending institutions, consumers, and mortgage brokers. A heightened awareness and more exacting standards in mortgage lending need to be employed to combat this increase in mortgage crime.

Types of Fraud

There are two types of mortgage fraud that are the most prevalent: identity fraud and value fraud.

Identity Fraud

There are many variations of identity fraud. In most cases, the fraudster impersonates the registered owner of the property in order to secure a mortgage against the land. For example, the fraudster electronically obtains information on the property and the registered owner, then transfers title into their name thus obtaining title to the land. If there is a registered mortgage on the land, the fraudster can also electronically create a false discharge of the mortgage.

Another variation of identity fraud includes fictitious employment records where the fraudster has created a fake letter of employment or has the number of the employer routed to a co-conspirator's phone number who confirms the false employment record. Another example includes the fraudster posing as the solicitor of a fake buyer for a transaction and stealing the funds instead of directing the funds to the buyer or non-existent seller.

Due to the ease and access provided these days by the internet and electronic transfers, identity fraud has increased rapidly in North America, along with the rise of other frauds, such as value fraud. There are a number of red flags that mortgage brokers should be cognizant of with respect to potential occurrences of identity fraud:

- the consumer does not provide photo ID upon request;
- the consumer has been involved in other offers that are "subject to financing" that have not gone through;
- the information contained at the Land Title Office is inconsistent with the mortgage application;
- the real estate transaction involves a relative of one of the real estate brokers;
- the buyers/sellers are not related, such as "Mr. Jones and Ms. Sweeney – joint tenants";
- the full name (first and last) of the buyer or seller is not disclosed on the application;

- the buyer's employment report does not match industry standards;
- the buyer has several investment properties, but no primary residence;
- the buyer's cheque does not match their identity;
- the down payment or deposit is in cash form;
- the person signing the application has been granted power of attorney by the real registered owner;
- appointments are all arranged via cell phone, fax or email and the meetings are held in public locations; or
- the buyer is involved in other real estate transactions with high ratio mortgages.

Value Fraud

Value fraud in mortgage transactions involve an artificial inflation of the price of a piece of property. The artificial increase can be produced by "flipping the property" or a false assessment/appraisal.

One "flip" scenario occurs when the fraudster purchases a home from an innocent seller for a certain price, i.e., $100,000 and then resells the property for a higher price to a co-conspirator for $200,000. The second buyer (co-conspirator) arranges for a mortgage equivalent to 95% of the purchase price ($190,000). This amount is applied to pay off the first purchase and the rest is left in the hands of the fraudsters who eventually stop making mortgage payments. The lender is then forced to foreclose and sell the property where they will not realize the full amount remaining on the mortgage since the house price was inflated beyond its actual value.

A different version of the flip involves the utilization of a fake appraisal. The fraudster purchases the property and then acquires or creates a false appraisal. The fraudster then sells the house to a buyer who can qualify for large mortgage. The final buyer who is not involved in the fraud is assured that their investment is sound by receiving the false appraisal. Once the buyer goes to sell the house, they realize the value is over-inflated and must continue to make high mortgage payments on a property whose value is lower than the mortgaged amount.

The red flags that mortgage brokers should be conscious of in order to spot value fraud include:

- the appraisal is missing or does not make sense;
- the appraisal was conducted by one of the parties involved in the transaction or is somehow connected to one of the parties;
- the appraiser is not on the approved list of appraisers for the lender;
- there is a vendor take-back mortgage on the property;
- there are a number of trades on the property in a short period of time;
- the final purchase price is higher than the listing price;
- the property contains illegal suites; and
- goods/chattels are used as part of the purchase price or deposit.

There are other general red flags that create suspicion and warrant a thorough investigation into value, identity, or some other type of mortgage fraud that may be present in the particular mortgage transaction:

- there are unique commission plans or simply low commission rates;
- the seller buys and sells many properties;
- there is one lawyer that represents both the buyer and seller;
- there is a condition on the agreement for purchase and sale that allows the buyer to show the property to prospective tenants, especially when requesting a high-ratio mortgage since most high-ratio mortgages must be owner-occupied;
- anything unusual occurs with the MLS® listing such as the property is removed prior to sale;
- there is an immediate possession date;
- there are no counter-offers;
- it seems like names have been erased or added to the application;
- one or more of the parties have not signed the contract;

- the agreement for purchase and sale indicates that both parties signed the contract at the same time; or
- the contract has been amended and the respected addendums and/or schedules are missing.

The Victims of Mortgage Fraud

The victims are spread across many fields. Obviously, the lenders and insurers have the most to lose financially with mortgage fraud. The *Gill v. Bucholtz* 2009 BCCA 137 case reinforces the problems for lenders as they must now bear the cost of fraud if they lend money to a registered owner who acquired their interest through fraud or forgery. However, those losses in turn are directed at future insurance customers in the form of steeper rates and premiums. Consumers also lose as they, and other innocent victims, are forced to spend time, effort, and legal fees to recover lost property.

There are also many non-financial losses worth mentioning that are incurred by the parties involved and also by their professions in general. With mortgage fraud on the rise, the real estate industry as a whole is scrutinized by the rest of the professional and consumer industries. Reputations and the credibility of real estate professionals including mortgage brokers are questioned regarding their due diligence standards and procedures, along with real estate lawyers and their attention to detail regarding individual transactions. More and more now, real estate transactions are becoming less hands on and are capable of completion with limited one-on-one interaction.

Mortgage fraud is becoming more accessible to fraudsters and therefore is becoming a larger threat to current and future home-owners. There are ways to prevent this fraud from occurring along with warning signs to look out for in order to put out the sparks before there is a fire.

Prevention Techniques

Since mortgage fraud investigations are time consuming and expensive, the professionals involved in real estate transactions must be educated, must practice certain techniques, and must conform to high standards of due diligence in order to prevent and avoid mortgage fraud to the greatest possible extent.

As noted above, red flags must be identified as soon as possible and followed up on closely in order to determine whether there is a possibility of mortgage fraud. For this to transpire, communication between members of various professional groups such as lending institutions, real estate lawyers, and mortgage brokers is key.

All of the professional industries involved in mortgage transactions play an important role in combating mortgage fraud. Lenders must make sure that proper due diligence standards are in place, and must report any justified suspicion of fraud promptly to the authorities. Mortgage brokers in particular play a key role in matching lenders with consumers and therefore mortgage brokers have a responsibility to know who their clients are and confirm their identity.

Mortgage brokers should practice a few of the following strategies in order to decrease the likelihood of mortgage fraud. Mortgage brokers:

- are responsible for ensuring that there are no inconsistencies in the application. They must confirm the identity of mortgage consumers at the beginning of the transaction and therefore know what is considered to be good identification versus easily manufactured identification;
- must demand identification personally from the applicant(s);
- must ensure that the information contained in the application (such as age, income, profession) is consistent with the information provided in the credit report;
- must ensure that the personalized void cheque contains a current address;
- with respect to employment letters, should perform an electronic directory verification of the employer's name, address and telephone number, and ask to speak to the "individual responsible for verifying employment";
- should confirm that the employer's name on the letter matches the information contained on the credit report;

- must request documentation with regard to large recent deposits;
- if the deposits were gifted, should confirm the giftor's name and address;
- should obtain a copy of the contract of purchase and sale;
- should ensure that mortgage applications requesting over 85% loan-to-value are owner-occupied;
- should acquire a municipal tax assessment and pictures of the property if it is a private sale;
- should conduct a telephone interview if the application is not completed face-to-face; and
- are to ensure that payroll deposits, bank statements, and tax documents (e.g., Notice of Assessment) are consistent and accurate with each other and reasonable with regard to the level of income being disclosed (e.g., consistent deductions on paystubs).

ALERT

From the Office of the Registrar of Mortgage Brokers:

Mortgage brokers need to recognize that lenders rely on the information they receive regarding potential borrowers. Mortgage brokers cannot say that it is not their responsibility to verify the information being given to them during the application process. Lenders indicate they assume that mortgage brokers have verified the information before forwarding it on. This office takes the position that a mortgage broker has a duty to ensure the information being sent to a lender has been verified.

Although no one is suggesting that mortgage brokers need to conduct in-depth investigations of every transaction that they process, reasonable due diligence must be undertaken to ensure that the information being passed on to lenders is accurate. Applications containing errors or omissions need additional verification and under no circumstances should brokers be referring applications that have been shown by another mortgage broker or lender to contain false or inaccurate information. If mortgage brokers do not verify the information they are forwarding to lenders, then mortgage brokers should advise the lenders in writing that none of the information has been verified.

Your cooperation and diligence will result in the mortgage broker industry continuing to maintain a professional and respected image in the community.

Source: MB 04-005 Misleading Information, October 2004

ALERT

Mortgage brokers can face steep penalties if they are found to have submitted false or inaccurate information to lenders in support of a mortgage application. In regulatory proceedings against a submortgage broker in 2013, the Registrar ordered that the submortgage broker pay $45,000 as an administrative penalty. The submortgage broker admitted to submitting numerous mortgage applications containing false information, handling falsified documentation in support of numerous mortgage applications, failing to conduct reasonable due diligence in the financial circumstances of her clients by not confirming unusual/suspicious financial information, and receiving remuneration as a result of arranging four mortgages while she was not registered as a submortgage broker.

Source: *www.bcfsa.ca/media/231/download*

THE *COMPETITION ACT*

The *Competition Act* (the "Act") is a federal statute designed to hold business actors accountable for misleading, deceptive, or anti-competitive practices. The Act is administered and enforced by the Competition Bureau, an independent federal law enforcement agency that is headed by the Commissioner of Competition. While the Act applies to all commercial activities, only the provisions most relevant to mortgage brokers will be discussed in this chapter.

The Act contains both criminal and civil prohibitions. Some offences (e.g., misleading advertising) are "dual track", meaning that they can be found in both the civil and criminal sections of the Act. The Act also permits private parties to sue for losses that result from conduct that is contrary to the Act. In short, a single violation of the Act could result in both a criminal record and civil liability for losses caused to injured parties.

For mortgage brokers, the most relevant provisions are those that address agreements in restraint of trade (section 45 and 90.1) and misleading advertising (section 52 and 74.01). Sections 45 and 52 are the criminal versions of these offences, while sections 90.1 and 74.01 are civil offences. Mortgage brokers should also be familiar with the provisions against price maintenance, a civil offence found in section 76 of the Act. Ignorance of the law is not a viable defence where a breach of the Act is alleged. Accordingly, it is important that mortgage brokers are aware of the Act and the provisions discussed next.

Criminal Provisions

Misleading Advertising/Deceptive Practices

Section 52(1) deals with false or misleading advertising. Section 52(1) states that:

> No person shall, for the purpose of promoting, directly or indirectly, the supply or use of a product [including mortgage brokering services] or for the purpose of promoting, directly or indirectly, any business interest, by any means whatever, knowingly or recklessly make a representation to the public that is false or misleading in a material respect.

If prosecuted as an indictable offence, a conviction is punishable by a fine in *any* amount at the discretion of the court and/or up to a maximum of fourteen years in prison. If prosecuted as a summary offence, the maximum penalty is a fine of $200,000 and/or up to one year in jail.

In determining whether the representation is “false or misleading in a material respect”, the courts will employ a two-step test. First, the court will consider both the literal meaning and the “general impression” that is conveyed to consumers by the representation. When assessing the “general impression” of the advertisement, the court will consider the nature of the intended audience, the medium of communication used, and any disclaimers that are present. Second, the court will determine whether this impression is misleading in a material respect. To do this, the court will consider whether the representation would have a real effect upon an ordinary consumer’s buying decision. There is no need to prove that an individual consumer or group of consumers was actually misled. However, “mere puffery” (e.g., claiming that product X is ‘the best in the world’) is not sufficient to constitute a material misrepresentation. Similarly, a minor misstatement (e.g., understating the maximum amount of a mortgage loan that a lender is willing to advance to a borrower by less than $500) would not likely be considered a material misrepresentation.

The general impression test is particularly important where the oral or written statements in the representation are literally true but the visual portion may create a false impression (e.g., a picture depicting a different model of the advertised product).

It should be noted that the forms of advertising covered by section 52 are extremely broad, including representations “by any means whatsoever”. This means that representations in print, oral, and digital form, including those posted to social media websites, are all subject to the Act. Mortgage brokers must be careful to ensure that the literal meaning and the general impression conveyed by all representations, in whatever form, are accurate. In some cases, this may mean that disclaimers or other qualifications are required.

As with all criminal offences, the Crown has a burden of proving a violation of section 52 'beyond a reasonable doubt'. In this case, that includes proving that the accused made the false representations knowingly or recklessly. Because of this requirement, the accused may escape liability under section 52 if they honestly believed that the representations or advertisements were not false or misleading and that they exercised due diligence in making sure that was the case.

Agreements in Restraint of Trade

Section 45 of the Act makes it a criminal offence for competitors to agree, arrange, or conspire with one another to:

(a) to fix, maintain, increase or control the price for the competitors' product (which can include services such as mortgage brokering services);

(b) to allocate sales, territories, customers or markets for the production or supply of the product; or

(c) to fix, maintain, control, prevent, lessen or eliminate the production or supply of the product.

As section 45 is a criminal offence, the Crown must prove the guilt of the accused "beyond a reasonable doubt". In the mortgage brokerage context, typical breaches of section 45 would include agreements among brokers, brokerages, or lenders to:

- restrict the types of services offered, such as credit consulting services;
- prohibit the advertising of commission rates or otherwise to control advertising activity (other than misleading advertising);
- prohibit certain types of inducements;
- control the entry of registrants or firms into the mortgage brokerage market; and/or
- setting fees for specific services.

Also relevant are the provisions of section 49(1) of the Act, which specifically apply to federal financial institutions (such as chartered banks). Section 49(1) makes it a criminal offence for federal financial institutions to make agreements or arrangements with one another fixing things such as:

- interest rates on mortgages;
- service charges;
- amount or kinds of mortgages;
- types of services;
- classification of borrowers; and/or
- any other terms related to mortgage loans.

Each mortgage brokerage must be free to set its own commission rate or fee with lenders and/or clients. Moreover, under the Act, it is illegal for individual registrants or firms to get together to set rates or fees, where the effect of such an agreement would be to lessen competition unduly.

Civil Provisions

As mentioned above, the Act contains both civil and criminal offences. On application by the Commissioner of Competition, civilly reviewable matters may be adjudicated by the Competition Tribunal, an independent adjudicative body. The Tribunal may make a remedial order where the offender is prohibited from performing the contravening conduct, or it may require an offender to take any other action determined appropriate. Unlike the criminal provisions discussed above, finding a violation of a civil offence only requires proof on a “balance of probabilities”, which is a lower burden of proof than the criminal standard of “beyond a reasonable doubt”. In other words, the Tribunal must be convinced that it is more likely than not that an alleged violation occurred.

Misleading Advertising/Deceptive Practices

The civil provision contained in section 74.01 is substantially similar to the criminal section concerning misleading advertising (section 52, discussed above). Under section 74.01, the representation must be misleading in a material respect, but there is no requirement to prove that the deceptive practices were made knowingly or recklessly. For this reason, most misleading advertising cases will proceed under this section. Under 74.01, the court may order a person to stop the activity, publish a notice, and/or pay an administrative monetary penalty. On the first occurrence, individuals are liable to a maximum penalty of $750,000 and corporations are liable to a maximum penalty of $10,000,000. These penalties increase for subsequent offences. Courts may also make restitutionary orders, whereby they order offenders to compensate consumers who suffered losses because of the deceptive practices.

Agreements Between Competitors

Some agreements between competitors may not be violations of the criminal provisions in section 45, but may nevertheless substantially lessen or prevent competition in a market. Section 90.1 of the Act allows the Competition Tribunal to review agreements or arrangements between competitors in order to determine whether the agreements or arrangements prevent, lessen, or are likely to prevent or lessen competition in a market. If the Tribunal finds that an agreement or agreement does this, the Tribunal may make orders requiring the competitors to do or stop doing anything with respect to the agreement or agreement. Unlike the sanctions imposed for criminal agreements under section 45, there are no penalties of fines or imprisonment under section 90.1.

Price Maintenance

Section 76 of the Act makes it a civil offence to discourage the reduction of prices, place upward pressure on prices, or discriminate against someone because of their low pricing policy, by means of threat, promise or agreement. The situations in which section 76 of the Act would be applicable to mortgage brokers and brokerages would include, amongst other things, the following:

- one or more brokerages “directly or indirectly” seeks to either have a rival mortgage broker raise its rates or fees or not reduce them below a certain level;
- a bank or other lender agrees to not cooperate or do business with one or more mortgage brokers or firms due to their fee structure.

FIDUCIARY AND AGENCY RELATIONSHIPS OF MORTGAGE BROKERS

Introduction to Fiduciary Relationships

In certain circumstances, a mortgage broker may enter into a special legal relationship with a client, known as a fiduciary relationship. In a fiduciary relationship, one party, the *fiduciary*, must act in the best interests of another party, the beneficiary. Under the common law, fiduciaries owe a duty of loyalty to the beneficiary, and must put the interests of the beneficiary ahead of all others, including the mortgage broker's own interests.

Certain categories of relationships are automatically presumed to be fiduciary relationships, such as lawyer-client or doctor-patient relationships. The mortgage broker-client relationship is not an established category of fiduciary relationships under the common law. However, even if a particular relationship does not fall into an established category, it is still possible for that relationship to be considered a fiduciary relationship, in which fiduciary duties (which will be discussed later) are owed to the client. Simply put, in order for two persons to be in a fiduciary relationship:

fiduciary
a person who holds a position of trust with respect to someone else and is obliged, by virtue of the relationship of trust, to act solely for the other person's benefit

1. the first person must have undertaken to act in the best interests of the second person;
2. the second person must be vulnerable to the first person's actions, in the sense of the first person having some power or control over them; and
3. the first person must have the ability to act in a way that could negatively affect the second person's legal interests or their substantial practical interests.[4]

If these criteria are present in a particular relationship, the relationship may be found to be a fiduciary relationship. In other words, it is possible for mortgage brokers to enter into fiduciary relationships with lenders or borrowers by fulfilling the three criteria above. If this occurs, then the mortgage broker will owe fiduciary duties to the lender or borrower, such as the duty of loyalty and the duty to avoid conflicts of interest. The courts treat breaches of fiduciary duties very seriously. If a mortgage broker is sued in civil court for breaching their fiduciary duties, the court will examine the relationship to determine whether or not it meets the aforementioned criteria. If the relationship is found to be a fiduciary relationship, then the mortgage broker may be liable for breach of fiduciary duties.

Introduction to Agency Relationships

An *agent* is a person authorized to act on behalf of another person, called the principal. The essence of the agency relationship is that the agent has the authority to act on behalf of the principal in dealings with others. Because agents are expected to be loyal to their principal and put the interests of their principal before all others, a mortgage broker who acts as an agent for a client may also be found to be in a fiduciary relationship with that client. However, a mortgage broker can be in a fiduciary relationship with a person (by satisfying the aforementioned criteria) without being an agent of that person.

agent
at common law, an agent is any person who contracts to act for or on behalf of another, who in turn, is known as the principal

Example

A mortgage broker promises to find the best possible mortgage product for a borrower. They also promise to help the borrower fill out the mortgage loan application properly. The borrower trusts the mortgage broker and follows their guidance and instructions. When the mortgage broker finds a suitable lender, the borrower submits the loan application directly to the lender. The mortgage broker does not deal with the lender on behalf of the borrower.

In this example, the mortgage broker is not authorized to represent the borrower in their dealings with the lender. Therefore, the mortgage broker is not the borrower's agent. However, the mortgage broker is likely in a fiduciary relationship with the borrower because:

1. the mortgage broker has represented that they will find the best possible mortgage for the borrower, amounting to a promise to act in the borrower's best interest,

2. the trust that the borrower has put in the mortgage broker means that the mortgage broker has some power or control over the borrower and the borrower is vulnerable to the mortgage broker's actions, and
3. the mortgage broker could act in a way that negatively impacts the borrower's legal or practical interests, such as by recommending a bad mortgage product that results in financial harm to the borrower.

The remainder of this chapter will look more closely at how mortgage brokers may enter into fiduciary and agency relationships with others, what the common law requirements are to create an agency relationship, and the fiduciary duties that apply to fiduciaries (including agents who are fiduciaries).

Mortgage Brokers as Fiduciaries and Agents

As discussed in Chapter 2, the term "mortgage broker" is broadly defined under the MBA. Some activities that require a mortgage broker registration are unlikely to give rise to fiduciary relationships. For example, a private lender will rarely be found to be in a fiduciary or agency relationship with borrowers. This is because it is generally understood that a lender acts for their own best interests, not the borrower's best interests. For the same reason, mortgage brokers who buy and sell mortgages on their own behalf are also unlikely to be fiduciaries. Similarly, a mortgage administrator who carries on the business of collecting mortgage payments is clearly not a fiduciary or agent for a borrower; rather, they are collecting payments from the borrower on behalf of the lender.

The mortgage brokering activity that is most likely to create fiduciary or agency obligations is mortgage arranging. This includes mortgage arrangers who assist borrowers and mortgage arrangers who assist lenders. This is especially true if a mortgage arranger takes on the role of trusted adviser to their client.

That said, it is important to reiterate that not all relationships established by mortgage arrangers will be fiduciary or agency relationships. Mortgage arrangers have a choice in determining the types of relationships they enter into. Some mortgage arrangers may be comfortable entering fiduciary or agency relationships with others. For example, some borrowers view their mortgage broker as an advisor, and may trust their broker to act in their best interests during the mortgage arranging process. Such borrowers may refer other borrowers to the mortgage broker in the future, and may return to the broker repeatedly in the future. Mortgage brokers may be comfortable establishing fiduciary or agency relationships with such borrowers, and may view it as good business practice to do so. In this case, mortgage brokers may provide assurances to borrowers that they will act in the borrower's best interests in the mortgage arranging process.

On the other hand, mortgage arrangers who wish to avoid entering fiduciary or agency relationships should avoid suggesting (orally, in writing, or by their actions) that they will put the interests of the client before all others. They should also ensure that the client is making decisions independently, based on all of the relevant information. In addition, suppose a certain client appears particularly vulnerable (in the sense that the mortgage broker has significant influence, control, or power over them and not necessarily because they belong to a vulnerable class of people), overly-trusting, or overly-reliant on the mortgage broker. In these cases, there is a higher risk of the broker-client relationship being fiduciary in nature. This may necessitate greater precautions by the mortgage broker to ensure that the client understands the true nature of the relationship. A mortgage broker may wish to recommend that a particularly vulnerable client obtain legal advice regarding a mortgage transaction. This may help avoid the suggestion that the client was vulnerable to the mortgage broker. Unless the mortgage broker is willing to act as a fiduciary, clients should not be given the impression that the broker is working solely for them or as their agent. This could occur inadvertently. For example, a mortgage broker may say to a borrower, "my goal is to find the best mortgage for you", or "I'm on your side, not the lender's", or "you don't need to worry, I'm taking care of everything". Comments like these may unintentionally lead the client to misunderstand the nature of the broker-client relationship, and cause the client to think of the mortgage broker as their agent or fiduciary.

As a Mortgage Broker...

Some brokerages may want to avoid entering into fiduciary or agency relationships with clients. For this reason, some client service agreements set out the nature of the services to be provided by the mortgage broker and specifically state that the mortgage broker is acting as an independent contractor and not as a fiduciary or agent of the borrower. Client service agreements may also state that the mortgage broker will have separate contractual agreements with various lenders. By addressing these items in client service agreements, brokerages can better control if and when they enter into fiduciary or agency relationships with consumers. However, it is important for mortgage brokers to conduct themselves in way that is consistent with the terms of the service agreement when actually serving clients. For example, if the service agreement states that the mortgage broker is not acting as a fiduciary, then the mortgage broker must avoid giving clients the opposite impression (e.g., by saying things like "trust me, I will get you the best interest rate and mortgage terms available"). If a mortgage broker behaves in a way that is inconsistent with the wording of the client service agreement, this may undermine the protections offered by the service agreement. It could also confuse consumers and lead to civil or regulatory liability for the mortgage broker. For example, a court could find that the mortgage broker was in fact in a fiduciary relationship with the client, despite the terms of the service agreement.

There have been several cases in which courts have examined whether mortgage brokers entered fiduciary or agency relationships with others. It is useful for mortgage brokers to keep these cases in mind while performing their business activities, so that mortgage brokers can be aware of when they may be entering into fiduciary or agency relationships with others.

Mortgage Genie Inc v. Johnson, 2014 CanLII 26813 (ON SCSM)

In this case, a mortgage broker was approached by a borrower who was facing foreclosure proceedings. The second mortgage on the borrower's property had fallen into default, and the borrower needed funds to repay that loan. The mortgage broker met with the borrower and had her sign documents for a new high-interest second mortgage. However, the new second mortgage was with a company that was owned by the mortgage broker, resulting in a conflict of interest. Later, the borrower refused to proceed with the new high-interest second mortgage, and the mortgage broker sued the borrower for its commission. The Court refused to order the borrower to pay the mortgage broker's commission, as it was determined that the mortgage broker was in a fiduciary relationship with the borrower. The Court described the borrower as "retired, elderly, and frail", and found that the borrower was relying on the mortgage broker to make the best possible mortgage arrangement for her. Therefore, she was vulnerable to the mortgage broker's actions. The Court determined that the mortgage broker was not entitled to his commission because he breached his duty to act in the best interests of the borrower by:

- failing to explore all of the borrower's options and failing to suggest the best possible arrangement for the borrower;
- steering the borrower towards a high-interest loan with the mortgage broker's own company;
- failing to disclose the conflict of interest – a printed statement in one of the documents that "Lender is an affiliated or related company of the brokerage" was insufficient disclosure;
- having the borrower sign a document promising to pay the mortgage broker his fee even if the defendant later refused to accept the mortgage from the mortgage broker's company; and
- not recommending that the borrower obtain independent legal advice on the mortgage documents, especially due to the conflict of interest in the transaction and the vulnerability of the borrower.

Mortgage brokers should be particularly mindful of their actions when assisting persons who may be vulnerable as a result of their age, level of financial sophistication, or health. All else being equal, a mortgage broker will be more likely to enter a fiduciary relationship when assisting these types of individuals than when assisting individuals who are not vulnerable in those ways.

Mortgage brokers may also enter into a fiduciary relationship with persons who trust the guidance of the mortgage broker, and view the mortgage broker as a financial adviser.

Pryce v. Vuckovich, [1999] O.J. No. 20 [Ontario Court of Justice (General Division)]

This case, which was discussed earlier in this chapter, is an excellent example of how a mortgage broker may become a fiduciary by assuming the role of trusted advisor to their clients. The basic facts of this case were discussed earlier and will not be repeated here. However, the following passages from the Court's judgment help highlight how a trusting working relationship can lead to the formation of a fiduciary relationship.

> It is clear from the evidence that the relationship that developed between [the mortgage broker] and the Pryce family was more than professional. Starting with her being social friends with Edie in the 1980's, the relationship developed into one of reliance and trust in [the mortgage broker] by other members of the family. This is evidenced clearly in a note written by Edie to [the mortgage broker] on June 18th, 1990 (at a time even after the Vuckovich mortgage was running into difficulties) in which she thanks [the mortgage broker] for "the loving care you take of our financial lives" and she ends the letter with "We love you". A note from Allan written some time in 1990 to [the mortgage broker] states I "thank you from the bottom of my heart for the things you do for me". And, Andre Bindseil, in a letter dated December 1990, closed with the remarks, "With loving greetings".
>
> With the death of Marcia Pryce and the substantial legacy that fell into the hands of particularly Joy and Edie, a dependency upon [the mortgage broker] developed and they relied upon her assurances that [the mortgage broker] would assist in investing their money in good and safe investments. [The mortgage broker] had familiarity and knowledge with the Pryce family's assets that only an insider would have and she knew of their relative inexperience in handling large sums of money and in investing in mortgages. It is clear that the hallmarks of influence, vulnerability, trust, confidence and dependence all existed in [the mortgage broker's] relationship with the Pryce family and the latter looked to [the mortgage broker] to act in their best interests. Accordingly, [the mortgage broker] assumed the role of a fiduciary.

As mentioned previously, the mortgage broker was held personally liable for the sisters' loss and ordered to compensate them on the basis of negligence.

Mortgage brokers who are willing to assume the role of trusted advisor to their clients should understand that by doing so, they may be entering into fiduciary relationships with those clients.

Mortgage Brokers that were not Fiduciaries

While the cases discussed previously both involved mortgage brokers who were found to have entered fiduciary relationships with others, there have also been cases in which mortgage brokers were not found to be fiduciaries. For example, in *Canadian Western Trust Co. v. Balakshin*, 2008 BCSC 798, the plaintiff (Canadian Western) was given information about a mortgage investment opportunity by the defendant mortgage broker. Canadian Western chose to invest in a third mortgage on the property, but lost its investment when the property was later foreclosed upon. The Court found that the relationship between Canadian Western and the mortgage broker was not fiduciary in nature. The mortgage broker had no discretion or power over Canadian Western in the transaction, Canadian Western was not vulnerable, and Canadian Western did not rely on the mortgage broker's expertise. In fact, Canadian Western was also a registered mortgage broker, with years of experience in the field. The Court found that Canadian Western was well aware of the risks involved in the investment and made a calculated choice to invest based on the information they had. This case is a useful example of how simply providing information to a lender about a mortgage investment, without controlling or otherwise influencing the lender's decisions, may not be enough to create a fiduciary relationship between the mortgage broker and the lender.

In a similar vein, a client who does not trust or rely on a mortgage broker may be unable to later argue that they were in a fiduciary relationship with that mortgage broker. In *Rescon Financial Corp. v. New Era Development (2011) Inc.*,[5] the Court stated that there was little trust, confidence and reliance placed by the borrower in the mortgage broker, and thus, there was no fiduciary relationship. In that case, there was many instances of the borrower second-guessing the mortgage broker's advice, or ignoring it entirely.

In summary, it may be less likely that a mortgage broker will be found to be a fiduciary if their client does not place great trust and reliance upon the mortgage broker. This is because the trust and reliance placed in the fiduciary by the beneficiary is a hallmark of fiduciary relationships. In addition, if the mortgage broker simply provides information to the client and does not exercise control over the client's decision making, it may be less likely that a fiduciary relationship will be found to exist. *Lindner v. Williams*,[6] was another case in which a mortgage broker was found not to be a fiduciary. The Court in that case stated, "what is missing here is a bestowing upon [the mortgage broker] the power to make decisions for the plaintiffs. [The mortgage broker] provided them with information. They made the decision. A claim for breach of fiduciary duty has not been made out."

AGENT'S APPOINTMENT AND AUTHORITY

As mentioned earlier, while a mortgage broker does not need to be an agent in order to be a fiduciary, if a mortgage broker becomes an agent, then the mortgage broker may also become a fiduciary, given that agents are generally required to act in the best interests of their principal. As a result, it is worthwhile to examine how a mortgage broker may become an agent under the common law.

Capacity to Act as an Agent

Generally speaking, any person of sound mind can act as an agent. Because an agent is not a party to the contract between the principal and a third party, the agent does not need the capacity to contract in order to enter into a contract on behalf of a principal. For example, an infant may act as an agent. However, an agent is a party to an agency agreement and, therefore, an infant agent could use their own incapacity to repudiate the agency agreement.

With respect to mortgage brokers, there is one important limitation on capacity. Anyone in British Columbia offering mortgage brokerage services must be registered under the MBA. Therefore, if a person wishes to act as an agent for another person in a mortgage arranging transaction, the agent must be registered under the MBA in order to be able to act as an agent.

Creation of Authority

Under an agency contract, the agent is given authority to do certain things on the principal's behalf in return for a fee or commission. The principal's promise to pay the agent must be supported by consideration or be given under seal. The agency relationship is normally created: (1) expressly; (2) by implication; (3) as a result of the doctrine of estoppel; or, (4) by ratification by the principal of the agent's acts done on the principal's behalf.

Express Contract. Most agency relationships are created by an express agreement which may be written or oral. In British Columbia, there are no statutory requirements for an agency agreement or the like (e.g., a written service agreement) between a mortgage broker and a client; however, a mortgage broker may choose to use a service agreement to outline their services, the nature of the relationship, and the form of compensation the broker may receive.

As a Mortgage Broker...

The verbal representations that you make to your client may be considered an oral agreement; therefore, use caution when communicating your role and services to your client. If you verbally represent yourself as an agent to your client, it may be binding and you will be expected to carry out the obligations and duties of an agent.

Additionally, if you intend to use a service agreement, you may choose to insert language in the document to advise your client that you are not acting as an agent in carrying out the services you are providing them. This alone is not definitive in determining whether an agency relationship exists; however, it may go towards proving your intent if called upon to do so.

Implied Agency. Agency can be implied by conduct. If one party has implicitly authorized another to act on their behalf, and the agent accepts this authority (even without realizing the consequences), the courts may determine that an agency relationship has been created by conduct.

Agency by Estoppel. Agency by estoppel arises when one person (the principal) makes representations to a third party that lead the third party to believe that another person (the agent) has authority to act on behalf of the principal. If a principal does this, and the third party relies on the representations, then the principal may be bound by the actions of their agent, even if there was no agency agreement between the principal and the agent.

Ratification. Sometimes an agent's authority can be granted retroactively. For example, an agent may enter into a contract on behalf of the principal, but the contract may be beyond the agent's authority. If the principal later consents to be bound by the unauthorized acts of the agent, the principal has ratified the contract. The result is that the principal is bound by the contract just as if the agent had been authorized to make the contract in the first place. Ratification of agency can apply whether an agent has acted without authority or beyond the scope of their authority.

Scope of an Agent's Authority

Once an agency relationship is established, it is necessary to examine the scope, or breadth, of the agent's authority. A principal will be bound to a third party only by acts that are within the agent's authority, unless the principal ratifies those acts. If an agent acts outside their authority, the agent may be liable to the principal for breach of the agency contract, or to a third party for breach of implied warranty of authority (explained later in this section). The authority of an agent may be actual or apparent.

Actual Authority. Actual authority is authority expressly given to the agent by the principal, for example in the agency agreement. Actual authority can also be provided in other ways, such as when a principal authorizes an agent to do something in an email or in some other form of communication. Additionally, if the specific words of an agency agreement or a principal's communication do not cover any particular circumstances, then the agent's actual authority may also include the implied authority to do anything necessary for, and ordinarily incidental to, carrying out the express authority granted to them. Additionally, if the agent's industry has any particular "customs of the trade", then the agent's actual authority may also include the authority to act according to those customs, as long as they are lawful and reasonable and the principal has not indicated otherwise.

Apparent Authority. Apparent authority is different from implied or usual authority. Apparent authority results from the operation of the legal doctrine of estoppel in circumstances where a reasonable third party would consider, from the conduct or statements of the principal and agent, that the agent did, in fact, possess authority. Agency by estoppel was discussed earlier.

Termination of Authority

Because the relationship between principal and agent depends upon their mutual consent, either party can terminate the authority at will. However, this does not mean that the terminating party will be free of liability, for example for a breach of the agency agreement by terminating it before its expiry date. Authority can be revoked orally or by conduct. For example, an act of the principal that is inconsistent with the continuation of authority would terminate the agency.

The agency relationship can also be terminated by operation of law. For example, the death, insanity, or bankruptcy of either principal or agent would terminate the agency. Consequently, if a corporate owner were to be dissolved, the agency would probably be terminated. The doctrine of frustration also appears to apply to the agency relationship.

COMMON LAW FIDUCIARY DUTIES

In earlier sections, a general introduction to fiduciary and agency law principles was provided, including a discussion of various cases in which these relationships were, and were not, found to exist. If a mortgage broker is found to be in a fiduciary or agency relationship (or both) with a client, then the mortgage broker will owe certain common law duties to that client. The law recognizes that, because beneficiaries place their trust and confidence in their fiduciaries, they may be particularly vulnerable to their fiduciaries' misconduct. As such, the law has special duties to ensure that fiduciaries (including agents who are also fiduciaries) do not abuse their position for their own interests or the interests of someone other than the principal. The following is a useful statement of the general duty of the fiduciary:

> When one party is obliged to act for the benefit of another, and the obligation carries with it a discretionary power, the empowered party becomes a fiduciary. A relationship with these attributes, however created, is marked by confidence and trust. Once created, equity will supervise the relationship by holding the empowered party to the fiduciary's strict standard of conduct. While its specifics may vary, this standard generally requires the fiduciary to act in a loyal and transparent manner in the beneficiary's affairs…[7]

As indicated in the quoted passage, a fiduciary's duties to their beneficiary (e.g., their client) may vary depending on the specific circumstances of the case. However, the general duty of a fiduciary is to be loyal to the beneficiary and to act transparently with respect to the beneficiary's affairs. The following duties are ones that are commonly owed by fiduciaries (including agents who are fiduciaries) to their beneficiaries:

1. the duty of loyalty;
2. the duty to avoid conflicts of interest;
3. the duty of full disclosure; and
4. the duty of confidentiality.

In addition, mortgage brokers who are agents also owe their principals a duty to carry out the lawful instructions of that principal.

The Duty of Loyalty

The overarching "umbrella" fiduciary duty is the duty of loyalty, which requires the agent to act solely for the benefit of the principal and put the principal's interests ahead of all others, including the agent's personal interests. The Supreme Court of Canada has stated that the duty of loyalty lies at the core of the fiduciary principle.[8]

The Duty to Avoid Conflicts of Interest

Fiduciaries have a duty to avoid conflicts of interest, where possible. Simply put, a conflict of interest arises whenever a mortgage broker, who is also a fiduciary, has the temptation to act in their own interest or a third party's interest rather than in the sole interest of their client (the beneficiary). The "conflict" for the fiduciary is between the duty of loyalty to the beneficiary and the motivation of the fiduciary to act for their personal gain or for the gain of a third party. If a conflict exists, the fiduciary must fully disclose the conflict and obtain the consent/permission of the beneficiary to proceed, in spite of the conflict. Otherwise, the fiduciary must stop acting in the conflict (which may even entail terminating the broker-client relationship).

It is worth repeating that not all mortgage brokers will become fiduciaries. A mortgage broker who is not a fiduciary does not necessarily have duty to avoid conflicts of interest under the common law (although they may have an ethical duty to do so, as discussed in Chapter 2. However, even mortgage brokers who are not fiduciaries are required to deliver a Form 10 (conflict of interest disclosure form) to borrowers and lenders under sections 17.3 and 17.5 of the MBA. As discussed in Chapter 2, these sections of the MBA require disclosure of any direct or indirect interest the mortgage broker or any "associate" or "related party" of the mortgage broker may acquire in the mortgage transaction.

Form 10 disclosure is concerned with conflicts of interest. For example, a commission payment from a lender creates risk that the mortgage broker will recommend that particular lender to a borrower to maximize their own commission, rather than because the lender offers the best mortgage product for the borrower. The purpose of Form 10 disclosure is to ensure that all parties working with the mortgage broker are aware of any competing interests that may affect that mortgage broker's advice or service to them. That said, it should be emphasized that a mortgage broker does not have to assess whether or not a conflict of interest actually exists in a transaction before making Form 10 disclosure. The MBA simply requires that the broker disclose all interests (direct and indirect) that exist in mortgage transactions. Disclosing all interests provides complete transparency to borrowers and lenders involved in the transaction. This allows each party to make their own assessment of the factors which may influence the broker acting in the transaction.

This is not to say that mortgage brokers need not concern themselves at all with conflicts of interest so long as Form 10 disclosure is made. In some circumstances, a mortgage broker may need to take additional steps to deal with a conflict of interest, apart from simply providing Form 10 disclosure. This is especially true if mortgage brokers have entered a fiduciary relationship with another person. Mortgage brokers who are fiduciaries cannot continue acting in a conflict of interest without, at minimum, fully disclosing the conflict and obtaining the consent of the client to proceed. However, a mortgage broker who is a fiduciary must always act in loyally and in the best interests of their client. Therefore, if the mortgage broker does not believe that they can fulfil this obligation due to a conflict of interest, then merely disclosing the conflict and obtaining the client's consent is not sufficient. The mortgage broker must tell their client that they are unable to continue acting for the client due to the conflict, and must stop providing mortgage brokering services to them.

Even mortgage brokers who are not fiduciaries may need to take additional steps to address a conflict of interest beyond simply disclosing it in a Form 10.

This is particularly true if the mortgage broker would be in contravention of the MBA if they fail to address the conflict.

Example

A mortgage broker is helping a borrower to refinance their mortgage and receives confidential information from the borrower that the borrower is undergoing divorce proceedings and is desperate to refinance. The broker is not in a fiduciary or agency relationship with this borrower. The broker is unable to arrange third party financing for the borrower. At this point, the broker offers to lend the borrower money themselves. However, knowing the borrower is desperate, the broker offers financing on predatory loan terms.

In this example, the broker has used confidential information that they received from the borrower within the broker-client relationship for the broker's personal financial benefit. Even though the broker in this example was not a fiduciary and did not owe a duty of loyalty to the borrower, BCFSA could still view this conduct as unconscionable or prejudicial to the public interest, which would constitute a breach of the MBA. If BCFSA took this view, Form 10 disclosure by the broker would not be enough to avoid regulatory sanctions. In this situation, the prudent course of action may be for the broker to not loan money to the borrower to avoid any suggestion that the broker took advantage of the borrower's confidential information about their personal circumstances. Alternatively, the broker could loan the borrower money while ensuring that the terms of the loan are not predatory. However, this second option creates significant risk for the broker. If the broker wants to proceed with a non-predatory loan to the borrower, then the broker should recommend the borrower to obtain legal advice about the loan, to ensure that the borrower understands the transaction and avoid the perception that the broker has taken advantage of the borrower.

Submortgage brokers should consult their designated individual about any concerns they may have about how to appropriately address conflicts of interest in their practice. BCFSA recognizes that competing interests are not always avoidable, and that the existence of a conflict does not necessarily mean that the mortgage broker has committed any wrongdoing. However, since conflicts have the potential to influence the objective performance of a mortgage broker's duties to their clients, they should always be approached with caution.

The Duty of Full Disclosure

A fiduciary must tell their beneficiary everything within the fiduciary's knowledge that might be relevant to the beneficiary. The goal in making full disclosure is to ensure the principal has all the necessary information to decide whether they want to proceed with the transaction.

The duty of full disclosure is closely tied to the duty to avoid conflicts of interest. When a conflict of interest arises, it must be disclosed immediately by the fiduciary to the beneficiary. Undisclosed or partially-disclosed conflicts of interest are a common source of legal liability for fiduciaries, including mortgage brokers who enter fiduciary relationships.

That said, while a fiduciary must obviously disclose any conflicts of interest to their beneficiary, that is not the limit of what must be disclosed. As stated, the duty of full disclosure requires full disclosure of all relevant facts that may affect the beneficiary's decision with respect to the transaction. This is a very wide-ranging disclosure obligation, and mortgage brokers who are fiduciaries must always ensure that no relevant facts are kept from their beneficiary, regardless of how trivial the mortgage broker may feel those facts are. The duty of full disclosure continues at least until the fiduciary relationship is terminated.

In addition to this common law duty to disclose, the MBA requires certain types of disclosure to be made by mortgage brokers to lenders and borrowers, such as Form 9 (investor/lender information statement) and Form 10 disclosures. These disclosures are mandatory for all mortgage brokers, regardless of whether they are fiduciaries or not. Note, while the fiduciary duty of full disclosure may overlap with the statutory disclosures required under the MBA, there may be situations where the fiduciary duty of full disclosure may exceed the mandatory disclosure requirements under the MBA.

Example

A mortgage broker is helping a developer to obtain mortgage financing for a development project. The broker has entered into a fiduciary and agency relationship with the borrower. Under the broker's service agreement, the developer has agreed to pay the mortgage broker a fixed fee of $100,000 if the mortgage broker secures financing for the developer. The mortgage broker locates a private investor who is interested in the development property. The investor makes an offer setting out the investor's proposed terms for the mortgage loan. The developer is quite pleased with the investor's proposal.

However, the broker has heard from their colleagues that this investor is often willing to negotiate. The mortgage broker thinks to themselves that the developer could make a counter-offer and get a better deal on the loan terms. What are the mortgage broker's disclosure obligations in this example?

In this example, the mortgage broker would need to provide Form 10 disclosure to the developer (the borrower) and the investor (the lender) setting out the fee that the mortgage broker will earn in the mortgage transaction. Additionally, the mortgage broker will need to provide Form 9 disclosure to the investor setting out key information about the mortgage investment, unless the investor is a "sophisticated person" as explained in Chapter 2. However, in addition to these two statutory disclosures, the mortgage broker's fiduciary duties of loyalty and full disclosure would also require the mortgage broker to disclose to the developer everything that they know about the investor's negotiating strategy, and their belief that the developer could get an even better deal. This disclosure is necessary even though the developer seems happy with the initial offer from the investor. Remember, the mortgage broker must provide the developer with all relevant information that may influence the developer's decision. This includes the information the mortgage broker has about the investor's negotiating strategy. While the developer may not make use of this information (e.g., the developer may not want to make any counter-offers), it is not for the mortgage broker to decide whether or not the information should be disclosed. The mortgage broker must provide all relevant information to the developer and the developer must make their own decisions about what to do with it.

As a Mortgage Broker...

The statutory requirement to disclose all referral fees, or fees of a similar kind by whatever name called, that are relevant to the mortgage transaction, in the prescribed form under the MBA, may not be sufficient to meet the standard required under the common law for the duty of "fullest disclosure". If the mortgage broker is acting as an agent for the client, the mortgage broker should take additional steps to ensure the client understands:

1. The nature of the fee;
2. The amount of the fee; and
3. How it is calculated.

Lastly, the mortgage broker should obtain the client's express consent to the mortgage broker accepting the fee.

Beware: a mortgage broker who gives their client a disclosure form under the MBA is not relieved of the other common law disclosure duties to the client. The responsibility of proving that proper disclosure has been made rests upon the mortgage broker.

As a Mortgage Broker...

If you are in a fiduciary or agency relationship and are unsure about whether a piece of information would influence your client's decision, put yourself in your client's shoes and ask yourself whether it is something you would want to know if you were the client.

When in doubt, it's always better to share the information with your client. You could face disciplinary and/or civil action if you fail to disclose a piece of material information.

Another facet of complete disclosure is that a fiduciary is not allowed to disguise or conceal a fee from the beneficiary. The following court decision describes this duty and the consequences of not fulfilling it.

Advanced Realty Funding Corp. v. Bannink, 1979 CanLII 1681 (ON CA)

In this case, a mortgage broker was hired to arrange a mortgage for a borrower. The borrower signed a document described as a "commission and fee contract" with the mortgage broker. This contract stated that the borrower would pay the mortgage broker a commission and that the broker may receive a finder's fee from a lender. The mortgage broker successfully arranged a mortgage with a lender that would have paid a finder's fee. However, the borrower decided not to proceed with the mortgage. The mortgage broker sued the borrower for the commission that the borrower was required to pay under the contract. The Court dismissed the mortgage broker's claim. The Court stated that it was not enough for the broker to bury a reference to the finder's fee within the commission contract. The broker should have clearly explained the fee to the borrower, including how it would be calculated, and should have ensured that the client understood and expressly consented to payment of the finder's fee. Because the mortgage broker failed to do that, the borrower was not required to pay the mortgage broker's commission.

Courts do not allow fiduciaries to withhold relevant information from their beneficiaries. If the information relates to the transaction, the mortgage loan, the other party, or the property, then the fiduciary must disclose the information to the borrower, even if the information does not directly impact the beneficiary's financial interests.

THE DUTY OF CONFIDENTIALITY

Generally speaking, "confidential information" is any information about a client that is not available to the public. A fiduciary must not disclose a beneficiary's confidential information to anyone else without the beneficiary's consent.

When a mortgage broker is a fiduciary (including an agent who is a fiduciary) for a borrower, examples of information that should be kept confidential include:

- that the borrower is highly motivated to obtain a mortgage loan due to their personal circumstances;
- that the borrower is willing to pay a higher than market rate of interest; and
- that the borrower may experience significant hardship (financial or personal) if the loan application is not approved.

When a mortgage broker is a fiduciary (including an agent who is a fiduciary) for a lender, examples of information that should be kept confidential include:

- the lender's negotiating strategy;
- the lender's inexperience with mortgage loan investments; and
- that the lender is willing to accept more borrower-friendly loan terms.

A beneficiary's confidential information may only be revealed if the beneficiary gives the fiduciary the express permission to do so, and this permission should be obtained in writing. If a mortgage broker is unsure of whether certain information is confidential, the best course of action is to not disclose it and then ask the beneficiary for permission to disclose it (if disclosure is in the best interests of the beneficiary).

While most fiduciary duties end when the fiduciary relationship ends (e.g., the mortgage transaction completes), the duty of confidentiality does not terminate when the transaction completes. It continues to apply until the parties agree otherwise. For this reason, there may be situations in which a mortgage broker may have conflicting duties to two separate parties in a mortgage transaction, even though they are no longer in a fiduciary relationship with either of the parties.

Example

Eight months ago, Harpreet (a mortgage broker) was trying to arrange mortgage financing for Barry (a borrower) who wanted to buy an investment property. While helping Barry, Harpreet learned confidential information about him. Barry had a great job earning a good salary. However, Barry told Harpreet was that he had a terrible relationship with his boss and he was worried that he might be fired. Barry was not sure when, if ever, he would be fired, but he was very worried about this happening because he believed that he would earn a much smaller salary at a different job. Harpreet entered into a fiduciary relationship with Barry while she was helping him. After a few weeks, Harpreet was unable to arrange any financing for Barry and so terminated the client relationship with him. A few days ago, Harpreet was approached by Ina, a private investor, who is looking for mortgage investment opportunities. Harpreet agrees to help Ina to find a mortgage investment opportunity and enters into a fiduciary and agency relationship with Ina. Today, Harpreet received a call from Ina. Ina tells Harpreet that her friend Barry just approached her. Barry told Ina that he is looking for a mortgage loan to buy an investment property. Ina knows that Barry has a great job, and also knows that the area in which Barry wants to buy the property is excellent. Ina would like Harpreet to arrange a mortgage on her behalf with Barry. What should Harpreet do?

In this example, Harpreet has conflicting duties to Barry and Ina.

- Harpreet is currently in a fiduciary relationship with Ina, and therefore owes Ina a duty of loyalty and a duty of full disclosure. If Harpreet were to comply with her duties to Ina, she would need to tell Ina everything she knows about Barry, including the potential issues with his job.
- On the other hand, even though Harpreet terminated her client relationship with Barry eight months ago, Harpreet still owes Barry a duty of confidentiality. This is because the duty of confidentiality continues beyond the end of the client relationship. Therefore, if Harpreet tells Ina what she knows about Barry's employment, she will be in breach of her duty of confidentiality to Barry.

In this situation, Harpreet should consult with her designated individual about how to manage her conflicting duties. If Harpreet wants to continue representing Ina in the mortgage transaction between her and Barry, Harpreet should take the following steps:

1. She must first consider whether she can continue acting for Ina in the circumstances. Harpreet should think carefully about the confidential information she received from Barry while acting as his fiduciary. Harpreet cannot disclose Barry's confidential information to Ina, her current client. Will this impair Harpreet's ability to represent Ina in the mortgage transaction? Arguably, it would. Ina seems to think that Barry

has a good job, and this is likely part of why Ina thinks this is a good mortgage investment opportunity. If Ina knew that Barry's relationship with his boss was shaky, this may very well change Ina's perception of the mortgage investment. Harpreet's inability to share this information with Ina is, therefore, impairing her ability to represent Ina in this transaction.

2. If Harpreet, after careful consideration, were to think that she could continue to represent Ina, then she must tell Ina:
   - Barry is Harpreet's former client with whom she had a fiduciary relationship; and
   - any confidential information Harpreet received from Barry while acting as his fiduciary cannot be disclosed by Harpreet to Ina, even if the information is material to the mortgage investment.

Again, a mortgage broker only owes common law duties such as the duty of loyalty and the duty of confidentiality to a person if the mortgage broker was in a fiduciary relationship with that person. Returning to the earlier example, if Harpreet was never in a fiduciary relationship with Barry, then she would not owe a common law duty of confidentiality to him, and could share what she knew about his job with Ina. However, even if the mortgage broker was never a fiduciary, and owes no fiduciary duties, to a former client, the mortgage broker should still avoid acting in a dishonest and unscrupulous manner towards that former client. Acting in a bad faith manner towards a former client could amount to conducting business in a manner that is prejudicial to the public interest or conducting business in a harsh, unconscionable or inequitable manner, both of which are contraventions of the MBA. Therefore, a mortgage broker who does not owe a fiduciary duty of confidentiality to a former client (because they were never in a fiduciary relationship with the former client) may still be liable for breaching the MBA if they misuse a former client's confidential information.

The Duty to Obey Lawful Instruction

A mortgage broker who is an agent is obligated to obey lawful instruction from their principal. This means that the agent must follow all instructions they receive from the principal, in order to act in the principal's best interest.

However, the agent is prohibited from acting upon instruction that would result in:

- a violation of federal, provincial or local law; or
- a breach of contract or other civil wrong.

THE DUTIES OF THE PRINCIPAL TO THE AGENT

While the bulk of the duties in an agency relationship are owed by the agent, the principal also owes limited duties to the agent. The two main duties of a principal to the agent are:

- the duty to indemnify the agent (i.e., to reimburse the agent for costs incurred by the agent in order to carry out their agency obligations); and
- the duty to pay (i.e., commission or a fee).

An agency agreement or written service agreement should contain a specific reference to indemnification, which requires the borrower to indemnify and save the agent harmless from all claims, damages, costs and liabilities incurred in connection with the services properly provided under the agreement.

An agency agreement or written service agreement should also contain clear terms on the commission or fee payable by the principal to the agent. Agreements with vague or uncertain remuneration language subject the agent to the risk of a court interpreting the term(s) in favour of the principal.

Select Mortgage Corp. v. 0856716 B.C. Ltd., 2012 BCSC 620

In *Select Mortgage*, the plaintiff mortgage broker claimed to be entitled to a fee of 2% of the amount borrowed from the defendant client, while the defendant alleged that he agreed to pay 1% or maybe a little bit more if the full amount sought was loaned. The client agreement signed by the parties stated that the broker "may be entitled to receive compensation." Before providing the client a letter of interest from a prospective lender, the mortgage broker prepared an invoice for the client to sign. The invoice initially provided for a 2.65% fee, but was replaced by the mortgage broker with a fee of 2%, as a result of what the mortgage broker claimed were negotiations as to the appropriate fee with the client. The copy of the invoice that the mortgage broker produced in court contained the client's signature. The client claimed that while he witnessed the mortgage broker changing and initialling the invoice to provide for a fee of 2%, he never agreed to this, nor did he sign the invoice (and he claimed he did not know how his signature ended up on the invoice). The client claimed that even with a change to a 2% fee, he objected, and that the parties later agreed to a 1% fee (and maybe more).

In a contest of credibility, the Court preferred the version of facts and events presented by the mortgage broker and ordered that the client pay a fee of 2% of the amount borrowed.

The *Select Mortgage* case highlights the risk of using vague clauses for remuneration in a written service agreement. Mortgage brokers should ensure that they explain the remuneration clauses in the service agreement and obtain the client's initials to any changes to the agreement. Brokers should also ensure that their clients receive a full copy of the executed service agreement.

RELATIONSHIP BETWEEN THE AGENT AND THE THIRD PARTY

Liability to a Third Party

It is important to appreciate that even in the situation where a mortgage broker has entered into an agency agreement with a client, the mortgage broker may still owe a duty to third parties in relation to the services provided. Whether or not a duty is owed to the third party will depend upon the circumstances of each case.

The three situations at common law when an agent can be personally liable to a third party are:

1. where the agent fails to disclose that they are an agent;
2. where the agent has no authority to act as an agent; and
3. where the agent commits a tort.

Failure to Disclose. Where an agent does not disclose to a third party that they are acting as an agent when entering into a contract, the agent may be held liable as a principal. This is only fair, because the third party has been led to believe it is making a contract with the agent personally, and might not have been willing to contract with the principal of whom the third party was never told. In this case, the injured party may choose to sue either the principal or the agent.

Example

Sam Shopper wishes to buy widgets, but he knows that Omar Owner will not sell to him. Sam employs Al Agent to buy the widgets for him in Al Agent's name. Omar Owner agrees to sell to Al Agent. But before completion of the sale, Sam Shopper goes bankrupt and is unable to produce the funds to enable Agent to complete. Al Agent will be liable for breach of contract if he does not complete because he was the party to the contract. If Al Agent later discloses that he was acting only as agent for Sam Shopper, Owner can choose instead make a claim against the assets of Sam Shopper under the general principles of agency.

No Authority. An agent who enters into a contract with a third party on behalf of the principal is presumed at law to have warranted or "guaranteed" that the agent has the authority to do so. A third party can rely on this warranty, known as the warranty of authority. Therefore, if an agent makes a contract with a third party on the principal's behalf without having the authority to do so, the agent may be liable for failing to live up to this "guarantee." The third party can sue the agent for damages in an action for breach of warranty of authority.

Commission of a Tort. An agent can never escape liability for torts committed by the agent on the basis that the agent was authorized by the principal to commit them. For example, if a borrower tells a mortgage broker to make certain representations concerning the borrower's financial status which are known to be false by both the borrower and the mortgage broker, the mortgage broker may be personally liable for fraud. The principal, of course, is also liable because the principal is responsible for the acts of their agent and the principal has expressly authorized the tort.

A principal is personally liable to an injured party for a fraud committed by the agent if the agent commits the fraud while acting within the scope of authority. This is true even where the principal does not authorize the fraud. It also does not matter that the fraud was committed solely for the agent's benefit (*Lloyd v. Grace, Smith & Co.* [1912] AC 716).

In fact, so strict is the liability of a principal, that even if a principal instructs the agent to disclose relevant information to a third party, if the agent fails to do so, the principal may be held vicariously liable to the third party for any damages resulting from the agent's misconduct.

MONEY LAUNDERING AND TERRORIST FINANCING

Introduction

Money laundering is an issue that affects all British Columbians. It harms economies, makes communities less safe, and negatively impacts society. When money from criminal activities is used to buy properties in British Columbia, it opens the door to more crime.

Money laundering is the process used to disguise the source of money earned from criminal activities. Essentially, money laundering is designed to convert “dirty” money into “clean” money. Criminals launder their money in order to enjoy the profits from their criminal activities, without raising the suspicion of law enforcement. Money laundering is a criminal offence in Canada under section 462.31(1) of the *Criminal Code*, which states that an offence is committed whenever someone deals in any manner with property or the proceeds of property with the intent to conceal or convert it, knowing or believing that some or all of it was obtained or derived as a result of the commission of a designated offence (e.g., drug trafficking, fraud, stock manipulation, tax evasion).

Money laundering is about more than “bags of cash”. A preconceived notion is that money laundered through real estate must involve a large payment of cash. In fact, most money laundering does not occur in the form of cash, as the dirty money has already entered the financial system electronically or by other means and is then transferred from a buyer to a seller.

Real estate transactions, including mortgage transactions, are highly attractive vehicles for money laundering. In order to combat the practice of money laundering in Canada, legislation such as the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (“PCMLTFA”) has placed numerous obligations on “reporting entities”, such as real estate salespersons/agents (known as “trading services licensees”), financial entities, real estate developers, accountants, casinos, and others. Under the PCMLTFA, all reporting entities must take certain steps and make certain reports to the Financial Transactions and Reports Analysis Centre of Canada (“FINTRAC”), which is a government agency responsible for collecting, analyzing, and disclosing information to law enforcement and national security agencies to combat money laundering and terrorist financing in Canada. Terrorist financing involves providing funds to support terrorist activity. Terrorist financers often use similar methods and techniques as money-launderers in order to conceal their criminal activity. The remainder of this chapter will focus primarily upon money-laundering.

As a Mortgage Broker...

Mortgage brokers and submortgage brokers are not currently reporting entities under the PCMLTFA, and therefore do not have FINTRAC reporting obligations. However, mortgage brokers are uniquely situated within the cross-section of the real estate and finance industries, and are more likely than the general population to encounter and observe money laundering activities. Mortgage brokers often interact directly with consumers in the course of their business. As professionals with “boots on the ground”, mortgage brokers are often well situated to identify suspicious activity, if and when it occurs.

Additionally, the more professionals who take part in the fight against money-laundering, the better the chances of detecting and deterring such activity. It is also important to note that, regardless of legal reporting requirements, mortgage brokers and submortgage brokers have a professional and ethical duty to help maintain public confidence in both the mortgage brokering and financial services industries. That duty includes being alert to indicators of potential money laundering and knowing the steps to take when red flags are observed. It is also important to understand that the due diligence a mortgage broker is expected to perform to detect and prevent mortgage fraud or misrepresentation may be very similar to the due diligence involved with detecting and preventing money-laundering. This is because there is a connection between money-laundering and mortgage fraud, which will be discussed later. Finally, while many financial institutions (such as banks and credit unions) are subject to PCMLTFA obligations, mortgage brokers may work with certain types of private lenders who may not have PCMLTFA obligations. Such lenders may represent a larger money-laundering risk than PCMLTFA regulated lenders, like banks.

The Scope and Impacts of Money Laundering

Money laundering has been identified as a problem both globally, and in British Columbia. The United Nations Office on Drugs and Crime has estimated that the amount of money laundered globally in one year is 2-5% of the global GDP, or $800 billion to $2 trillion US dollars. In their report, *Combatting Money Laundering in BC Real Estate* (the "Expert Panel Report"), the authors conservatively estimated that annual money laundering activity in 2018 in Canada was $46.7 billion, of which $7.4 billion was in British Columbia. It has been estimated that money laundering in the British Columbia real estate market has increased real estate prices by 5%. In fact, one particular money laundering tactic was so prevalent in British Columbia that it was labelled the "Vancouver Model" by the international community. Vancouver has been ideal for money laundering because of its highly desirable real estate, its traditionally welcoming attitude towards high-stakes gambling, the density of money transfer companies, and the high demand for illegal drugs.

There are many negative impacts of money laundering, including that money laundering:

- may lead to increased corruption of public officials, and threaten the "rule of law": the accountability of all persons, institutions, and entities under the law;
- can erode the public trust of professionals who assist money launderers;
- facilitates and encourages criminal activity;

- is linked to tax evasion, which deprives governments of funds to provide essential public services; and
- causes distortions in the market, particularly by inflating the prices of assets that are attractive to money launderers.

In November 2020, as part of its efforts to combat money laundering in this province, the British Columbia government established the Commission of Inquiry into Money Laundering in British Columbia, headed by Justice Austin Cullen of the British Columbia Supreme Court (the “Cullen Commission”). The Cullen Commission’s mandate was to inquire into, report upon and make recommendations with respect to money laundering in British Columbia, The Cullen Commission has conducted hearings and reviewed various evidence, including reports such as the Expert Panel Report. In June 2022, the Cullen Commission released its final report, which is an 1800+ page document containing detailed information, analyses, and recommendations intended to address the issue of money laundering in various industries in BC, including the mortgage brokering industry.

Why Money Laundering Occurs in the Real Estate and Mortgage Industries

The Government of Canada’s 2015 “Assessment of Inherent Risks of Money Laundering and Terrorist Financing in Canada” (the “Inherent Risks Report”) found that the real estate sector is highly vulnerable to money laundering. The Financial Action Task Force has estimated that real estate accounts for nearly one-third of criminal assets confiscated worldwide. Mortgages are particularly attractive vehicles for money-launderers. While criminals often use mortgage fraud schemes to generate illegal profits, as discussed earlier in this chapter, money-launderers also use mortgage fraud schemes to launder dirty money. The Inherent Risks Report categorized mortgage fraud as a “very high” money-laundering threat in Canada, given the sophistication and capability of mortgage fraudsters, and the scope and magnitude (in dollar amounts) of criminal activity associated with mortgage fraud. Much of the mortgage fraud conducted in Canada is conducted by organized criminal groups with the witting or unwitting assistance of professionals in the real estate sector, including mortgage brokers. In his report, *“Money Laundering in Canada: An Analysis of RCMP Cases”,* Stephen Schneider found that of the 83 RCMP cases involving real estate, 63 (73.5%) involved the use of mortgages.

Real estate and mortgages are attractive to money launderers for a variety of reasons:

1. **High Value:** Real estate is a big-ticket, high value asset, meaning that large amounts can be laundered in a single transaction. By extension, mortgage loans are also high value transactions which offer the opportunity for large scale money-laundering.
2. **Security:** Real estate is a fairly secure and stable asset that cannot be physically stolen and is less susceptible to dramatic decreases in value in the long term. Mortgages are also considered a relatively safe investment given that the underlying security for all mortgage loans is real estate.
3. **Simplicity:** There is a large market for real estate and mortgage loans, and entry into these markets does not require a high degree of sophistication (when compared to investing in stocks or other financial instruments, for example).
4. **Potential for Profit:** Real estate typically increases in value in the long term, and renovations and physical improvements can add to the profit potential of a property. Further, mortgage loans generate interest payments, providing a return on investment.
5. **Various Methods to Launder Money:** Money can be laundered through real estate in multiple ways, including the use of separate legal entities in real estate purchases/sales, and unregulated lenders in financing real estate.
6. **Subjective Value:** Since no two properties are exactly alike, prices can be manipulated to control the amount of money laundered in a transaction.
7. **Oversight:** Some participants in the real estate and mortgage industries are unregulated, or under-regulated, meaning that there are “weak spots” in the industry that criminals can exploit.
8. **Scrutiny:** Some types of mortgage transactions may involve less scrutiny over borrower income and wealth and investor capital than others. For

example, private mortgages sometimes involve less verification of a borrower's income than mortgages from a federally regulated bank or a provincially regulated credit union.

9. **Anonymity:** The identity of *beneficial ownership* of real estate can be hidden through the use of corporations, trusts, and *nominees*. Similarly, corporations, trusts, and nominees can be used in mortgage-related money-laundering schemes such as the "loan-back" scheme (discussed later), in order disguise the criminal origin of loan funds. Mortgage brokers should note that in November 2020, the *Land Owner Transparency Act* (LOTA) was brought into force in British Columbia as part of the government's broader efforts to combat money-laundering, tax evasion, and fraud in the province. LOTA aims to make ownership of BC real estate more transparent by requiring certain beneficial ownership information about BC real estate to be filed in a searchable registry, known as the Land Owner Transparency Registry. By tackling hidden ownership of real estate, LOTA seeks to make real estate a less attractive vehicle through which to launder money.

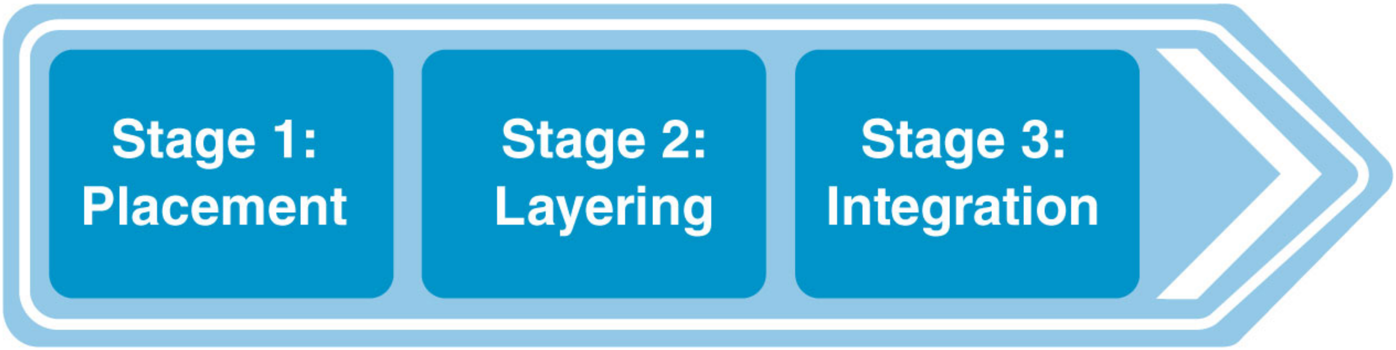
beneficial owners (generally)
individuals who enjoy the benefits of ownership of property even though the property is registered in the name of another person or entity

nominee
an individual or entity that is legally registered as the owner of property, with true control and ownership belonging to one or more other, unregistered persons or entities (also known as a "bare trust" arrangement).

10. **Speculative Component:** Because short-term ownership of real estate is not unusual, criminals can flip properties as part of their money laundering activities without necessarily raising suspicion. Value fraud schemes also occur in the mortgage industry due to the speculative nature of real estate.

The Money Laundering Process in the Mortgage Industry

FIGURE 5.1: Stages in the Money Laundering Process



As shown in Figure 5.1, there are three stages in the money laundering process. The first stage is placement, which is the process of placing the proceeds of crime into the financial system. Criminals are vulnerable when they possess large amounts of cash that can link them to an underlying crime, so by placing it into the financial system, they are better able to transfer and manipulate their funds. The next stage is layering, which is the process of converting the criminal funds into another form in order to conceal the criminal origins of the proceeds. The final stage is integration, which involves reintroducing and reintegrating the laundered funds into the legitimate economy to create the perception of legitimacy and having the funds appear to have been legally earned.

Example of Money-Laundering Stages in a Mortgage Transaction: Private Lender

Placement	A private lender involved in money-laundering makes several cash deposits into their bank account, over a lengthy period of time. The deposits never exceed $9,500 so as to avoid large cash transaction reporting requirements under the PCMLTFA. The deposits are derived from criminal activity. This is an example of placement.
Layering	The private lender uses the illicit funds accumulated in their account to advance a mortgage loan to an innocent borrower. Borrowers may seek out private loans if they have credit issues or are otherwise unable to qualify for loans from lending institutions such as banks or credit unions. The borrower pays monthly mortgage payments of clean money to the private lender over time. Later, perhaps after the borrower's credit improves, the borrower discharges the private loan by refinancing with a chartered bank. The chartered bank pays the new loan proceeds funds into its lawyer's trust account. The lawyer discharges the private mortgage from title, replaces it with the bank's mortgage, and pays out the private lender's loan with clean money from the trust account. Through these transactions, the money-launderer has created distance between the criminal activity that generated the illegal funds and the layered funds.
Integration	The private lender uses the clean money to acquire assets, such as real estate, or to invest in further mortgages and earn additional income.

There are many different methods used by criminals in order to launder money within the mortgage industry. Mortgage brokers should understand the types of schemes used by criminals so that they are better equipped to identify money-laundering activity if and when they encounter it. Some examples of money-laundering schemes in the mortgage context include:

1. **Mortgage Payments with Dirty Money:** Criminals may obtain a mortgage loan from a private lender, and while the down payment may be made with legitimate funds to avoid scrutiny, the mortgage payments may be made with dirty money. Even if the lender is regulated, mortgage payments are usually subject to less scrutiny than bank deposits because they are usually in smaller amounts and are made over time in a predictable manner.

2. **Quickly Discharging Mortgages:** A related technique is to repeat the mortgage repayment process multiple times with a series of quickly discharged mortgages. In this method, the criminal obtains a mortgage loan (clean money), quickly pays it off with proceeds of crime (dirty money), and then applies for, and obtains, another mortgage loan (clean money). This process allows the criminal to launder more money more quickly.

3. **Loan Back Schemes:** A criminal can lend themselves money from their own illicit funds to finance a real estate purchase. They could use companies or nominees (e.g., family members or other trusted associates of the money-launderer) as the lender to create the appearance that the loan has come from someone else, in order to make the mortgage transaction seem more legitimate.
4. **Acting as Unregulated Private Lenders:** Criminals can launder dirty money by operating as unregulated private lenders, similar to the scheme illustrated previously. The loan repayments from innocent borrowers represent clean money, allowing the money-launderer to distance their money from its criminal origins.

It can sometimes be difficult to differentiate money-laundering transactions from legitimate transactions. However, mortgage brokers should exercise caution when one or more of the following characteristics are present in a particular transaction, as they may signify that money-laundering is occurring:

1. **The mortgage involves a lender is who is not required to report to FINTRAC.** Mortgage brokers should be especially vigilant when dealing with borrowers who appear unusually interested in working with these alternative lenders, as they often offer borrowers less desirable loan terms (e.g., higher interest rates) than other lenders who have FINTRAC reporting obligations.
2. **The transaction involves a mortgage which is being discharged relatively quickly after it was first obtained.** Similarly, a borrower or property that has had many mortgages registered and repaid in quick succession may also indicate money-laundering activity. Obtaining and quickly repaying mortgage loans may allow criminals to launder fairly large amounts of dirty money relatively quickly.
3. **A mortgage has characteristics which do not seem appropriate in all of the circumstances.** For example, a mortgage may have a very high loan to value ratio (representing high lender risk), but the borrower may have insufficient provable income to justify that ratio. Alternatively, a relatively low-risk loan may have a relatively high interest rate. These “mismatches” could suggest that the borrower and lender have some

type of prior relationship with one another. This relationship may simply be family members or friends helping each other financially. However, it may also be a relationship to facilitate money-laundering, such as the "loan back" scheme discussed earlier.

4. **The lender or borrower wishes to arrange a large number of mortgages within a short period of time.** This may be an indication that the person wishes to launder a large amount of money fairly quickly.

Steps Mortgage Brokers Can Take to Combat Money-Laundering

As previously discussed, money-laundering is a major issue in our society and mortgage brokers have a professional and ethical duty to be alert to potential money-laundering in the course of their business, and take appropriate steps to address money-laundering if they suspect it may be occurring. If submortgage brokers suspect or believe that they are encountering money-laundering activity, submortgage brokers can report the activity to one or more of the following entities, depending on the circumstances of the transaction:

1. **The brokerage's designated individual:** As discussed in Chapter 2, the designated individual is responsible for ensuring proper supervision, registration, and recordkeeping of all employees and transactions of the mortgage broker. Submortgage brokers should not hesitate to raise money-laundering concerns or suspicions activity with their brokerage's designated individual in order to obtain further guidance.
2. **FINTRAC:** As discussed previously, FINTRAC is responsible for collecting and analyzing data from various reporting entities under the PCMLTFA, for the purposes of combatting money-laundering. While mortgage brokers are not required to report to FINTRAC, any person may voluntarily report suspicious activity to FINTRAC in order to assist it in its mandate.
3. **RCMP:** Money-laundering and terrorist financing are criminal activities and, as such, can be reported to law enforcement. The RCMP has programs and initiatives in place to investigate and combat these activities in order to improve the safety and security of Canadians.

4. **BCFSA:** If a money-laundering scheme involves a mortgage broker, BCFSA has the authority to take regulatory action against that mortgage broker, since participation in money-laundering activity could constitute conducting business in a manner prejudicial to the public interest, or other contraventions of the *Mortgage Brokers Act*.
5. **Borrowers or lenders:** depending upon the circumstances, a mortgage broker may have a duty to inform innocent borrowers or lenders if a particular transaction may have some connection to money-laundering. For example, a mortgage broker who knowingly assists a money-launderer to arrange mortgages with unsuspecting private lenders could be exposed to regulatory liability, legal liability, and other negative consequences such as reputational damage, unflattering news media coverage, and so on.

Further, a prudent mortgage broker can take preventative steps to mitigate money-laundering risks before such risks can even occur. Mortgage brokers may wish to develop anti-money laundering programs in order to ensure that appropriate steps are taken in all transactions to identify, avoid, and report money-laundering activities in a timely and efficient manner. Designated individuals may consult with anti-money laundering experts in order to learn more about such programs and how to institute them within their brokerage. Additionally, many of the mortgage fraud prevention techniques discussed previously in this chapter will also help brokerages in the fight against money-laundering.

CONCLUSION

Chapter 5: "The Professional Liability of Mortgage Brokers" is organized into five key sections. First, you were introduced to a number of ways in which a mortgage broker, or other professional, may face liability. These sources of liability include negligence, misrepresentation, and breaches of fiduciary duties, to name a few. Second, mortgage fraud was introduced. Mortgage brokers can play a large role in minimizing mortgage fraud, which carries significant penalties. Being able to identify clients who may be engaging in mortgage fraud early in the process will help you avoid troublesome files. Next, Chapter 5 moved to a discussion of the *Competition Act*, which regulates how mortgage brokers and other entities compete with each other. After this, this Chapter introduced fiduciary and agency law, a breach of which may result in liability for the mortgage broker. Finally, Chapter 5 discussed the problem of money-laundering and what role mortgage brokers can play in fighting this criminal activity. As you can see, while being a member of a profession has many benefits, there are risks. Being aware of the types of risks, key red flags that may indicate risk, and who to consult when in doubt goes a long way in minimizing the risk of professional liability.

1 Information Bulletin – Misleading Information: *www.bcfsa.ca/media/1517/download*

2 Consent Order dated August 2, 2009: *www.bcfsa.ca/media/209/download*

3 [1999] O.J. No. 20 [Ontario Court of Justice (General Division)]

4 *Alberta v. Elder Advocates of Alberta Society*, 2011 SCC 24 paragraph 36

5 2018 ONSC 259 (aff'd 2018 ONCA 530)

6 2004 BCCA 243

7 *Mulligan v. Stephenson*, 2016 BCSC 1941 at para. 108.

8 *Hodgkinson v. Simms,* 1994 CanLII 70 (SCC).