

## **SOME ETHICAL ISSUES FOR REAL ESTATE LAWYERS**

Real estate law can be fertile ground for ethical issues with its practitioners. Real estate transactions are often very fast paced, with many issues to consider. Who is your client? What is your role as the real estate lawyer? How do you immerse yourself in a transaction, but remain able to balance the needs of your other clients? Who are you acting for in the transaction? How should you rely on other professionals in the real estate industry.

All of these questions need to be considered in each new file that you think about opening. Typically, the real estate practitioner is opening more files than his or her peers in other areas of the firm. Even where a real estate practitioner is restricted to working for only one client (as is the case of the in-house counsel), the volume of transactions and the variety of issues that can arise are large and wide.

The purpose of this paper is to bring attention to some of the issues that affect the typical real estate lawyer, whether they work in-house or in private practice. These issues are not meant to be exhaustive, but a starting point for further discussions.

### **1. Building a Successful Relationship with In-house Counsel**

As external counsel, there are many things to think about while working with in-house counsel. Of course, the ultimate goal for any real estate lawyer working in private practice is to develop and retain the business of the in-house counsel's company going forward. In-house counsel routinely judge external counsel on their technical abilities, responsiveness, breadth and depth of talent and judgment. However, perhaps even more important is the relationship that external counsel is able to cultivate with their in-house peers. It is often that personal relationship that wins the day on "beauty contests", assuming that the external counsel has met the mark on the relevant professional criteria. As a result, external counsel should focus on building a positive relationship with in-house counsel from the get-go.

One key to a successful relationship with in-house counsel is communication. Before beginning work on a matter, external counsel should ask as many questions as possible, both general and specific, in order to properly understand the nature of the work that in-house counsel would like

completed. It is important for external counsel to understand the work challenges, environment and industry that an in-house lawyer needs to manage and contend with. In-house counsel are often faced with questions from all directions, but the “top down” pressure from senior management is the most critical for an external counsel to appreciate and manage. If your in-house counsel needs to make a presentation to the board on a specific day, then that means that your advice is needed much sooner.

Also, knowing the scope of the external counsel’s required engagement/retainer on a matter is critical. There is nothing that will irritate in-house counsel more than receiving a bill for work that was already completed internally. In order to avoid an inefficient duplication of work, external counsel should establish the scope of the work in-house counsel would like them to complete. Also, external counsel should be aware of the company’s legal budget and use all efforts to stay within that budget unless they obtain explicit approval from the client. Keeping tabs on your time and knowing when you are outside of the previously agreed upon budget will allow you to advise your in-house counsel promptly. Together you may be able to trim work from other less important areas. At a minimum, it will allow your in-house counsel to advise its management team accordingly, in order to reduce friction over billings at the end of the transaction.

## **2. Managing External Counsel**

A primary duty of in-house counsel is the management of their external counsel. In many instances, the in-house counsel is having to defend his or her decision to use one law firm over other competitors in the market. There are many decisions that must be made, including when to involve external counsel, how to set up the fee structure and determining which counsel to use. It is likely that all these decisions will be made with cost in mind. External counsel services in general can be very expensive for companies. Accordingly, the first thing in-house counsel should do before reaching out to external counsel is to set a budget for an agreed upon scope of work.

In-house counsel must ensure that they hire the right external counsel. There are a number of things to keep in mind when shopping for the right legal team. While the list of qualities to look for are endless, there is nothing more important than reputation, track record and expertise.

Rates will no doubt be an important consideration. However, external counsel should keep in mind that getting the right advice in the beginning will save money in the long run; fixing “messes” which are created by inexperienced counsel can be costly. Even though the right external counsel might seem expensive to hire, it could save costs in the long run.

To control costs, in-house counsel should create guidelines. The guidelines should address cost estimates, budget concerns and matter staffing. For example, only junior lawyers should partake in research work and due diligence should be delegated to staff and paralegals. In-house counsel teams are sophisticated and experienced in how law firms operate: the lower level work should be pushed to the appropriate levels. Senior external counsel involvement in files should be limited to complex negotiations or strategic advice at critical junctures of the transaction.

Another consideration to keep in mind is whether to use alternative billing arrangements. This will depend on the kind of work given to external counsel to complete. If the work is not “standard form”, it would most likely make more sense to be billed based on time. However, many in-house counsel find great value from using a fixed fee arrangement. The billing arrangement in-house counsel chooses will be largely dependent on the external counsel and the type of work involved. Standard conveyance transactions, financings and lease negotiations in real estate law lend themselves well to fixed fee or alternate billing arrangements. For example, consider engaging a law firm to carry out all of the lease negotiations in a year for a national retail tenant for a fixed fee.

It is important to maintain a positive and strategic relationship with external counsel. This relationship can be built by regularly communicating business objectives, inviting external counsel to meet key employees at the company to better understand how it operates and by sharing feedback during the course of a matter or at its conclusion. As long as an open line of communication is maintained and concerns are raised early and honestly, many difficult situations will be easily resolved or avoided completely.

### **3. Common Fraud Schemes**

Fraud schemes are prevalent at all levels of the real estate market. It is important for real estate lawyers to be aware of these fraud schemes so they do not unknowingly become a participant.

The real estate lawyer is responsible for managing the real estate transaction as a whole, so he or she needs to be aware of any potential cases of fraud. Where is the money coming from? Where is the money being sent? Knowing your client and the origin of the funds can be important in order that you can discharge your obligations in a responsible, professional and ethical manner. If a transaction does not pass a lawyer's smell test, better to ask questions and dig into the concerns rather than ignoring everything and marching onward.

The *British Columbia Code of Professional Conduct* provides that, "a lawyer must not engage in any activity that the lawyer knows or ought to know assists in or encourages any dishonesty, crime or fraud, including a fraudulent conveyance, preference or settlement." Lawyers have a duty to be on guard against becoming the tool or dupe of an unscrupulous client. While there are dozens of fraud schemes that real estate lawyers should be aware of, we set out two of the most common schemes below.

One of the most devastating frauds for property owners is title fraud. In this type of fraud, the fraudster typically finds a property and poses as the owner. The fraudster will then register forged documents transferring the property to their name, and then get a new mortgage against the property or sell the property to an innocent purchaser. Once the rogue secures funds, he or she will disappear. In such cases, the rogue will provide the lawyer with false contact information and photo identification.

Value fraud is another common scheme. This type of fraud involves a rogue who agrees to purchase a property, usually at fair market value. The fraudster will then flip the property at an artificially higher value to an accomplice. Then, the new purchaser will attempt to obtain a new loan by deceiving a mortgage lender as to the true value of the property.

According to the Law Society of Upper Canada, if a lawyer is suspicious or has doubts about whether they are assisting a client in dishonesty, fraud, crime or illegal conduct, the lawyer should make reasonable inquiries to obtain information about the client and the subject matter and objectives of the retainer. A lawyer should also clarify the nature and purpose of a complex or unusual transaction where the purpose is not clear. Other tips to avoid becoming the tool or dupe of an unscrupulous client include: making conveyancing staff aware of the common

characteristics of real estate fraud, watching for urgency and waiting for funds to clear before paying out.

The most effective way for a lawyer to avoid fraudulent real estate transactions and schemes is to be familiar with client identification requirements. Over the last decade, every province and territory has adopted Know Your Client rules. These rules constitute a professional ethical obligation for lawyers and are monitored and enforced by the applicable Law Society. While Know Your Client rules are adopted slightly differently in each province and territory, the rules in each jurisdiction are structured around four primary obligations: identification, verification, record-keeping and withdrawal. Lawyers should be sure to review the Know your Client rules applicable within their own jurisdiction.

#### **4. Avoiding and Managing Law Society Complaints**

In British Columbia, almost a quarter of the complaints received by the Law Society arise from real estate related files. These complaints come primarily from dissatisfied clients and opposing counsel. Responding to a Law Society complaint is one of the last things any lawyer wants to do. Fortunately, a large portion of complaints that the Law Society receives are easily avoidable. Accordingly, we set out below some of the most common complaints and how to avoid them.

The most common complaint made to the Law Society involve lawyers failing to respond or communicate with their clients. These complaints can be avoided by simply managing client expectations. Clients often have preconceptions about how their transaction will proceed and how their lawyer should act. A client could be unsatisfied about a lawyer's performance during a transaction, while in the lawyer's mind, the transaction has been a success. Effectively managing the expectations of a client is essential for a successful solicitor-client relationship. In order to avoid these complaints, every lawyer should begin managing client expectations early, be familiar with the transaction in which they are engaged, follow up with the client in writing after all consultations and keep the client consistently informed. A successful lawyer will make sure that he or she gets back to clients promptly and keeps them informed as to the progression of their file.

Another common complaint is rudeness. In British Columbia, there are several rules in the *Code of Professional Conduct* which deal with the conduct expected of lawyers in their professional dealings. A lawyer's conduct towards clients and opposing counsel should always be courteous and any animosity between clients or other lawyers should not influence lawyers in their conduct or demeanour. It is important to keep this in mind during all interactions, no matter how stressful or frustrating the circumstances. Ultimately, courtesy and professionalism should rule the day in all of our dealings with clients and other counsel.

In most real estate practices, legal assistants and paralegals carry out a significant portion of work on files. Failure to properly supervise staff has led to many complaints against real estate lawyers. Lawyers should be aware that there are limits to the appropriate use of non-lawyers. Responsible lawyers should always maintain direct supervision over each non-lawyer staff member, maintain a direct relationship with the client and take full responsibility over the work being done by the non-lawyer staff. Also, lawyers should ensure all matters requiring professional skill and judgment are dealt with by a lawyer and that legal advice is only given by authorized persons.

The best way for lawyers to avoid complaints being made about them to the Law Society is to read and be familiar with their own jurisdiction's code of professional conduct. If a lawyer comes across a situation where they are unclear as to what the best ethical course of action is, they should seek advice from a practice advisor from their Law Society or from a benchler. These discussions will be confidential and can provide lawyers with sound advice and good peace of mind.

## **5. Representing Multiple Interests in Real Estate Transactions**

There are often times when a client will ask a real estate lawyer to represent both sides in a real estate transaction. Lawyers handling transactions other than real estate rarely even consider representing both sides in a transaction. However, when it comes to real estate transactions, there are scenarios that enable real estate lawyers to undertake joint representations.

Should a lawyer be asked to act for more than one party in a real estate transaction, it is important they carefully consider for whom they are being asked to act and what potential there

is for a conflict of interest. The jurisdiction's professional code of conduct should be strictly adhered to. Lawyers should be cautious even if the transaction appears to be straight forward with little potential for a conflict of interest.

In British Columbia, unless the transaction is a "simple conveyance", a lawyer should not act for both a buyer and a seller. The *British Columbia Code of Professional Conduct* provides examples of transactions that are considered simple conveyances:

- (a) the payment of all cash for clear title,
- (b) the discharge of one or more encumbrances and payment of the balance, if any, in cash,
- (c) the assumption of one or more existing mortgages or agreements for sale and the payment of the balance, if any, in cash,
- (d) a mortgage that does not contain any commercial element, given by a mortgagor to an institutional lender to be registered against the mortgagor's residence, including a mortgage that is
  - (i) a revolving mortgage that can be advanced and re-advanced,
  - (ii) to be advanced in stages, or
  - (iii) given to secure a line of credit,
- (e) transfer of a leasehold interest if there are no changes to the terms of the lease,
- (f) the sale by a developer of a completed residential building lot at any time after the statutory time period for filing claims of builders' liens has expired, or
- (g) any combination of the foregoing.

In Ontario, generally two lawyers are required for the transfer of title to real property. There are some circumstances recognized as not needing two lawyers to represent the buyer and seller as no real conflict exists. These circumstances include the transfer of title to simply change the

“legal tenure” and transactions where the transferor and transferee are related persons and “not at arms length”.

## **6. Relying on Other Real Estate Professionals**

Real estate transactions involve an array of professionals. Real estate licensees, inspectors, environmental consultants and appraisers often provide advice that is relied upon by purchasers or lenders. Accordingly, purchasers and lenders have legal recourse against these professionals if the property or security acquired is not as represented. In British Columbia and Ontario, there is a regulatory framework in which real estate licensees, appraisers and inspectors operate. Also, each of these professionals owe a duty to their clients, or, in some cases, to third parties. If rescission is unavailable or the sale has completed, a real estate lawyer should advise their clients to consider claims against the other real estate professionals involved in the transaction.

Real estate licensees acting for a buyer or pursuant to a dual agency agreement must know the property their principal is buying in order to advise them accordingly. A licensee’s failure to inform their principal about a material aspect of a property can be found as negligent.<sup>1</sup> A listing licensee has a duty to verify material facts about the property that is listed. This forms part of the listing licensee’s duty to exercise reasonable skill and care.

Inspectors have a duty to conduct inspections and prepare inspection reports in a competent and reasonable manner. Contracts often identify which professional guidelines apply to the inspector. However, these contracts only identify the minimum standards and even if the guidelines in the contract are met, a finding of negligence may still be possible.

Claims made against real estate appraisers for a misleading appraisal are assessed using the test for negligent misrepresentation found in *Queen v. Cognos*, [1993] 1 S.C.R. 87. This test is made of five parts which include: (1) a duty of care arising from the relationship; (2) representations that were untrue, inaccurate, or misleading; (3) those representations were made negligently; (4) the plaintiff reasonably relied on those representations; and (5) that reliance was detrimental in the sense that damages resulted. It is expected that appraisers will act with a reasonable degree of care, knowledge and skill in coming to their valuations. If an appraiser does not live up to this

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<sup>1</sup> *San-Co Holdings Ltd. V. Kerr*, 2009 BCSC 1747



standard, they will be found negligent. If an appraisal turns out to be wrong, the appraiser will not necessarily be found liable. However, a valuation off by a wide margin could be used as evidence of negligence.