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April 4, 2002

Oklahoma flip tosses lawyer

Properties simultaneously purchased, flipped but mortgage lender wasn't told

The Law Society of Upper Canada has sent a clear message to the legal profession that lawyers who participate in real estate flip transactions without making full disclosure of the facts to all parties, particularly the new mortgage lender, will no longer be permitted to practise law.

The issue arose in the recent Law Society discipline case against J. Paul Burk, 63, of Mississauga. He was found guilty of professional misconduct for his role in a series of what is commonly referred to as Oklahoma transactions.

An Oklahoma involves artificially increasing the value of a property so the mortgagee is left with security that may be partially or entirely worthless. The increase is often accomplished by a simultaneous purchase and resale (or flip) of the property.

The mortgage lender on the second transaction is not aware the property has been simultaneously purchased at a lower price, which can sometimes be less than the amount of the mortgage being advanced.

Last year, Bruce King of Sutton Group Results Realty in Burlington, a regular reader of this column, wrote to tell me the derivation of the name.

Apparently, the term Oklahoma became popular when oil barons were financing their rigs in the oilfields of that state. "Evidently it became necessary from time to time to obtain financing from lenders who were reluctant to invest in the risky business of oil speculation," King explained.

"Often, the landowner would report a property as an oil-producing rig when, in fact, it would turn out to be little more than a dry hole. This fact was not normally discovered until after the lender had financed the deal. I guess it happened with enough frequency that Oklahoma became synonymous with over-valued real estate."

However the term originated, it is no doubt used with increasing frequency in the offices of mortgage lenders who got stung by real estate flips orchestrated by Paul Burk's clients.

J. Paul Burk was found guilty of professional misconduct for his role in a series of what is commonly referred to as Oklahoma transactions.

The Law Society discipline panel that heard the case against Burk received a 53-page statement of facts signed by the lawyer, in which he detailed his clients' flips. The statement makes it clear that, aside from normal and modest legal fees, Burk did not otherwise profit from the transactions.

(I should also add at this point that, although I am an elected member of the Law Society's governing board, called Convocation, I had no role in the Burk case, and did not know anything about it until it was made public by the Law Society in late February.)

Except for the addresses and prices, the facts in each of the eight transactions in the Burk case were almost the same. There were two agreements of purchase and sale in each file. The original vendors and their lawyers entered into bona fide, arm's length transactions. They had no knowledge that each property was being flipped at a higher price.

Typical of the transactions was the house at 40 Ossington Ave. When the Law Society's auditors examined Burk's file, they found two agreements of purchase and sale. In the first agreement, a person named Jay Singh agreed to buy the property from the Ukrainian Credit Union. Its mortgage was in default, and it sold the property to Singh under the power of sale in its mortgage for $115,000. It had no knowledge of any resale of the property. In the second agreement, "J. Singh in trust" agreed to sell the same property to T. Ram for $195,000. Ultimately, both transactions closed on the same day in April 1996.

The credit union had its own lawyer, and Burk acted for three parties: the vendor J. Singh, the purchaser and borrower Tony Ram, and the new lender, Montreal Trust Company of Canada.

Based on his mortgage application, and believing the property had sold for $195,000, Montreal Trust approved Ram for a new first mortgage of $178,350.

Since Burk was the lawyer in the $115,000 transaction as well as the $195,000 transaction, and also represented Montreal Trust, he had an obligation to advise the lender about the first transaction at $115,000.

In his statement filed with the Law Society panel, Burk admitted he failed to disclose to Montreal Trust that he was also acting for Singh on the $115,000 purchase from the credit union.

On April 16, 1996 a deed was registered from the credit union to Singh at a price of $115,000. Moments later, he sold the property to Tony Ram for $195,000. Burk acted on both transactions. Immediately following the second deed, Burk registered Montreal Trust's first mortgage of $178,350.

Burk admitted to the panel that he knew but did not tell his client Montreal Trust that the value of the property could not support the amount of the new mortgage.

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He also acknowledged participating in the preparation of an affidavit, in which Ram stated a $21,000 down payment came from his own money.

When the smoke cleared, a mortgage of more than $178,000 had been advanced against a property that had been purchased for $115,000. From the surplus, Burk wrote a cheque for more than $53,000 after closing to a third party.

If all this seems complicated, it is. The end result of this and seven other transactions was that Burk's clients obtained properties with no down payment, large amounts of surplus funds were paid to third parties, and the new lender was left with a mortgage significantly higher than the value of the property.

The Law Society discipline panel agreed with Burk that his participation in the flip transactions amounted to professional misconduct. He was allowed to resign his membership in the Society, and ordered to pay costs of $5,000.

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