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Lawyer suspended for role in house flips

Homes sold twice to inflate their value before applying to bank for mortgage

The Law Society of Upper Canada has censured a lawyer who was involved in a series of 27 property flips, which cost the Royal Bank of Canada more than $458,000.

Between December, 1996 and January, 2000, Toronto lawyer Alexander Havrlant, 66, acted in a series of what's known as "Oklahoma" property flips where a property is bought from an innocent vendor at market price and then resold at an inflated price.

(In a typical Oklahoma property flip, a middleman buys a property and immediately resells it to a "dummy" purchaser at an artificially higher value. A bank finances the second purchase without knowing about the first transaction, and ends up holding a mortgage in an amount higher than the true value of the property. The purchaser effectively buys the property for no money down and pockets the difference between the true (lower) purchase price and the inflated bank mortgage.)

The facts in all but one of the Havrlant transactions are similar, and were admitted in a signed statement the lawyer provided to the law society.

According to Havrlant's statement, real estate agent Daniel Scott and associate Haywood Welton would buy, or find an associate to buy, a property from an unsuspecting vendor. Acting as a middleman, that person would then resell the property to an ultimate purchaser, also found by Scott or Welton.

Both transactions would close the same day. Former lawyer Peter Maloney would act for the ultimate purchaser and mortgagee, with Havrlant acting for the middleman, who would be a buyer and seller simultaneously.

Here's how it worked with a property on Woodfield Rd. Back in 1996, the innocent owner named Li sold the house to Jones for $104,000. Scott was the real estate agent for Jones, the purchaser, and Havrlant was his lawyer.

On the same day, Jones flipped the property to Banwell for $137,000. Without knowing about the $104,000 deal, the Royal Bank gave Banwell a 95 per cent mortgage on the higher value. Peter Maloney acted for Banwell and the Royal Bank. He did not advise the bank of the original $104,000 purchase and has since been permitted to resign from the Law Society. (See Title Page, May 31, 2003, at http://www.aaron.ca.)

When the smoke cleared, there was a profit of more than $25,000, which Havrlant paid to 1600 Pacific Place Holdings Ltd. Welton was one of the directors of the company.

Two and a half years later, the same thing happened again. Banwell sold the same property to Bradshaw for $168,000. CMHC provided mortgage financing of about $155,000, and the profit on that deal was about $24,000.

The Law Society file makes no reference to whether the Royal Bank conducted appraisals or inspections when it advanced both mortgages.

In November, 2000, a court-appointed receiver sold the Woodfield Rd. property, leaving the Royal Bank with a loss of almost $56,000.

This scenario was repeated on 26 other properties.

The essence of the Law Society's charges against Havrlant (which he admitted) was that he "aided and assisted in a scheme, orchestrated by ... Welton," involving the purchase and sale of properties and the payment of the profits resulting from mortgage financing to Welton's company. Strangely, there is no allegation that the transactions were fraudulent, or that the bank was duped.

The Society also alleged, and Havrlant admitted, that he failed to disclose to the intermediate owners the risks of participating in these transactions. This, too, is a puzzling allegation, as the "flipper" clients were presumably in on the bank scams, and wouldn't have been interested in such advice.

Three other charges against Havrlant related to a property on Sibley Ave. In this case, the Royal Bank knew about the original legitimate purchase because it provided financing for it.

The Royal advanced a 75 per cent mortgage based on the first sale price of $115,000 in December, 1997. Six weeks later, the property was flipped for $147,000 a jump of almost 28 per cent.

Knowing of the original deal (because it held a mortgage on the property) the Royal Bank provided the purchaser with 90 per cent financing insured by CMHC.

Havrlant acted for the intermediate and final purchaser, as well as the Royal Bank. He was charged by the Law Society with two counts of professional misconduct for failing to disclose to the bank that the property was being flipped for a profit.

While I do not condone his conduct, it is clear that Havrlant could not possibly have concealed anything since the bank held both the smaller and larger mortgage on the same property.

Properties are legitimately flipped for a profit all the time, but there is no allegation in the two Law Society charges against Havrlant that the Sibley Ave. flip was improper or fraudulent or at an inflated price. Nor is there any explanation of why it was misconduct for Havrlant to fail to disclose to the bank that it already had a mortgage on the property.

On April 14, 2003, a Law Society discipline panel chaired by Clayton Ruby suspended Havrlant from the practice of law for a period of nine months.

The Royal Bank now instructs lawyers acting on their mortgage transactions to alert them if the property has increased in value over a short time.