Financial Services Litigation Bulletin

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Negative Credit Rating for Customer Causes Negative Impact for Bank

The Ontario Court recently held that if a financial institution provides inaccurate information to a credit rating agency, it will have the same liability as the credit rating agency if the error is not quickly rectified when they are informed of it.

Clark applied for a personal loan in 1994 which was denied because of a R-9 credit rating for an allegedly unpaid loan from the Bank of Nova Scotia ("Scotiabank"). Clark subsequently contacted Equifax Canada Inc. ("Equifax"), a national credit-reporting agency, to inform it that this was an error and that he had no such loan with Scotiabank. Equifax assured him that the matter would be investigated and corrected if an error was found.

From 1994 to 2000, various banks informed Clark of the R-9 credit entry on his report. Notwithstanding this, Clark was repeatedly approved for various loan transactions. During this time period Clark claims to have contacted Equifax and Scotiabank several times to correct the error, but it was not until November 2000 that he put his complaint in writing.

In September 2000 Equifax contacted Scotiabank to investigate Clark's complaint. Shortly thereafter, Scotiabank confirmed that the delinquent loan was not attributable to Clark, but to another individual with a similar name and notified Equifax of the error. As a result, Equifax immediately corrected Clark's credit rating.

In analyzing whether the defendants were liable to Clark, the court referred to a recent decision of the Ontario Court of Appeal dealing with the duty held by credit reporting agencies to consumers. In that case, the Court of Appeal stressed the importance of credit and credit reporting in today's society. It held that it was reasonably foreseeable that if credit rating agencies are negligent in gathering information, their actions could cause credit grantors to deny credit or to charge more than they otherwise would. Therefore, credit reporting agencies had a duty to consumers to accurately report their credit information.

The twist that is added by this case is that the Court applied this reasoning to Scotiabank and found it liable on the grounds that it had supplied the erroneous information in the first place. No weight appears to have been given to the fact that Scotiabank could not have unilaterally corrected the error, as it did not have control over the credit rating report. Scotiabank was found to be equally liable with Equifax.

Although the damages in this case were limited to compensation for the distress that this error caused to Clark, the court clearly stated that if there was evidence of damage to financial reputation which caused monetary loss, Scotiabank could have been liable for that loss.

Implications of Decision

It is clear that the courts have developed a low tolerance for negligent credit mistakes and that they are going to hold financial institutions to the same high standard as credit rating agencies. Therefore, financial institutions must exercise care when reporting credit information and must be quick to fix errors when they are brought to their attention. Furthermore, this case implicitly demonstrates that banks should treat oral complaints just as seriously as written ones. Not only are there compelling business reasons to react quickly to complaints, whether oral or written, a failure to do so may also be a source of legal liability.

Clark v. *Scotiabank,* [2004] O.J. No. 2615 (S.C.J.)

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This bulletin was prepared with the assistance of Sandra Sbrocchi, Student-at-Law

Other Recent Cases

Lender Bears the Loss in Fraud Scheme

A commercial lender, National Holdings Inc. ("National"), agreed to provide a mortgage to an individual fraudulently claiming to be "Henry Cowan" the owner of a residential property. The funds were advanced by National to the fraudster's agent, who then issued a cheque to the fraudster in Mr. Cowan's name. The fraudster gave the cheque to a third party who charged the fraudster a fee to cash the cheque through his account at the Canadian Imperial Bank of Commerce ("CIBC"). The Court found that CIBC was not liable to National as National was not the owner of the cheque which was cashed by CIBC.

National Holdings Ltd. v. *Canadian Imperial Bank of Commerce,* [2005] B.C.J. No. 560 (S.C.).

Oral Evidence of Representation Admitted in Face of "No Representation" Clause

At issue was whether an alleged oral representation made by a banker raised a triable issue. The defendant guaranteed a loan made to a company, which subsequently filed for bankruptcy. The defendant claimed the guarantee was invalid because the Business Development Bank of Canada loan manager involved in the transaction had represented that the guarantee would only be relied upon if there was fraud in the transaction. The Court held that even though the guarantee contained a "no representation" clause which warranted that the parties would be bound by the terms of the written agreement and excluded liability for any pre-contractual presentations (the "No Representations Clause"), it would allow evidence of the oral representations. As a result of this evidence being admitted, the Court held that there was a genuine issue for trial as to whether or not the guarantee was valid. This is a timely reminder that even though most standard form loan documents include No Representation Clauses, these clauses may not always be enforceable.

Business Development Bank of Canada v. *Turack,* [2005] O.J. No. 1128 (S.C.J.).

Limitation Period Commences as Soon as Lender has Right to Accelerate Loan

The Business Development Bank of Canada (the "BDBC") advanced money to a company. The loan agreement provided that the BDBC had the right to accelerate the loan upon a default so that it would be immediately due and payable. In July 1996 the company defaulted, but the BDBC did not exercise its right to accelerate until October 1996. In October 2002 the BDBC commenced an action to recover the debt. The British Columbia Court of Appeal held that the six-year limitation period commenced when the BDBC had the right to accelerate in July 1996 and therefore the claim was statute barred. Therefore, those seeking to enforce loan agreements should be careful to calculate the limitation period from the date on which they have the right to call a loan and not when they actually do.

Business Development Bank of Canada v. *Papke,* [2005] B.C.J. No. 1091 (C.A.).

Independent Legal Advice Not Always Necessary

Mrs. Henein brought an action to set aside a mortgage made by Mr. Henein to the Bank of Nova Scotia ("BNS") against the matrimonial home. First, she claimed that her consent to the BNS mortgage was induced by the fraud and undue influence of Mr. Henein, to which BNS had knowledge. Secondly, she asserted that BNS should have also insisted she receive independent legal advice. The Court held that BNS did not have a duty to insist on independent legal advice because Mrs. Henein attended a law office where she swore that she was Mr. Henein's spouse and was consenting to the mortgage. Furthermore, the court did not find Mrs. Henein was under any undue influence. Although she was not enthusiastic about signing the mortgage, she admitted that she knew she was going to the law office to sign a mortgage, and that by signing it she was encumbering the house.

Henein v. *Henein,* [2005] O.J. No. 1921 (S.C.J.).

Who We Are

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Brett is an associate in the firm's Commercial Litigation and Corporate Restructuring Groups. He has a general corporate commercial litigation practice with an emphasis on financial institution litigation, insolvency and restructuring, debtor/creditor disputes and fraud. Brett regularly acts for financial institutions on a wide variety of litigation issues. Brett is also the editor of the firm's Financial Services Litigation Bulletin.

Financial Services Litigation

Our Financial Services Litigation Group acts for both domestic and foreign financial institutions on a wide range of matters. We represent our clients in collecting debts and enforcing security, including guarantees, priority claims, letters of credit and other financial instruments. We also handle *Bills of Exchange Act*, fraud and fraudulent conveyance, and auditors' negligence litigation, and defend financial institutions in class actions and in claims against them for breach of fiduciary duty, lender liability, breach of contract and breach of trust. We enhance our clients' representation by calling upon the broad expertise of our lending and insolvency solicitors as needed.

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