

A Primer for In-House Counsel

Corporate and Financial Crimes

Part 2 of 6

CRIMINAL FRAUD



Blakes

Introduction

In this six-part series on corporate and financial crimes, the Blakes Business Crimes, Investigations & Compliance group outlines basic principles of criminal and quasi-criminal law that may arise in the running of a business. Armed with insights from years of multidisciplinary knowledge and experience, our lawyers provide brief answers to questions that in-house counsel routinely ask relating to these issues.

If you would like more information or to discuss a specific issue, please contact any member of our Business Crimes, Investigations & Compliance group.

SERIES ON CORPORATE AND FINANCIAL CRIMES

1. Criminal Law 101
- 2. Criminal Fraud**
3. Bribery & Corruption Offences
4. Money Laundering
5. Securities-Related Offences
6. Competition

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What Conduct Gives Rise to Criminal Liability for “Fraud”?

The *Criminal Code* contains a number of offences that are directed at what have traditionally been viewed as “commercial” crimes. The one offence that warrants specific attention is criminal fraud. Based on how broadly Canadian courts have interpreted criminal fraud, this is an offence that potentially has the broadest application to conduct in a commercial setting. An understanding of the elements of this offence is therefore important for in-house counsel.

The offence of fraud is created by section 380 of the *Criminal Code* and is defined as follows:

Fraud

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,

- (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 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.

Minimum Punishment

(1.1) When a person is prosecuted on indictment and convicted of one or more offences referred to in subsection (1), the court that imposes the sentence shall impose a minimum punishment of imprisonment for a term of two years if the total value of the subject-matter of the offences exceeds one million dollars.

Affecting Public Market

(2) Every one who, by deceit, falsehood or other fraudulent means, whether or not it is a false pretence within the meaning of this Act, with intent to defraud, affects the public market price of stocks, shares, merchandise or anything that is offered for sale to the public is guilty of an indictable offence and liable to imprisonment for a term not exceeding fourteen years.

THE PROHIBITED ACT

The prohibited act that makes up the offence of fraud consists of two distinct elements:

1. a prohibited act of deceit, falsehood or other fraudulent means. In the absence of deceit or falsehood, the courts will look objectively for a “dishonest act,” i.e., what a reasonable person would consider to be a dishonest act; and
2. a deprivation must be caused by the prohibited act. The deprivation must relate to property, money, valuable security or any service.

THE MEANING OF “DISHONEST”

The broad definition of fraud encompasses objectively “dishonest” conduct. Where there has not been a deliberate deceit or falsehood, the question becomes what is “dishonest” such as to give rise to potential liability for fraud? Is it dishonest to take advantage of a loophole or gap in a contract that the other party failed to notice when they signed the contract? Can an organization that has entered into a “bad” deal complain that it has been dealt with “dishonestly”? Is it dishonest to enter into a contract through a corporate entity rather than personally so as to limit liability? Is there a duty on a seller of property to disclose facts to the other party that are material to its price if no inquiry is made? The answers to such questions are not always clear.

The Supreme Court of Canada has not provided an exhaustive definition of what constitutes fraudulent conduct, though it has provided some guidance. In *R. v. Zlatic*, McLachlin J. (as she then was) defined “dishonesty” as follows:

... Dishonesty is, of course, difficult to define with precision. It does, however, connote an underhanded design which has the effect, or which engenders the risk, of depriving others of what is theirs. J. D. Ewart, in his *Criminal Fraud* (1986), defines dishonest conduct as that “which ordinary, decent people would feel was discreditable as being clearly at variance with straightforward or honourable dealings” (p. 99). Negligence does not suffice. Nor does taking advantage of an opportunity to someone else’s detriment, where that taking has not been occasioned by unscrupulous conduct, regardless of whether such conduct was wilful or reckless. The dishonesty of “other fraudulent means” has, at its heart, the wrongful use of something in which another person has an interest, in such a manner that this other’s interest is extinguished or put at risk. A use is “wrongful” in this context if it constitutes conduct which reasonable decent persons would consider dishonest and unscrupulous.¹ (emphasis added)

In *R. v. Théroux*, McLachlin J. provided the following description of whether conduct is “dishonest”:

The requirement of intentional fraudulent action excludes mere negligent misrepresentation. It also excludes improvident business conduct or conduct which is sharp in the sense of taking advantage of a business opportunity to the detriment of someone less astute. The accused must intentionally deceive, lie or commit some other fraudulent act for the offence to be established. Neither a negligent misstatement, nor a sharp business practice, will suffice, because in neither case will the required intent to deprive by fraudulent means be present.²

1 [1993] S.C.J. No. 43 at para. 32.
2 [1993] S.C.J. No. 42 at para. 40.

THE REQUIRED DEPRIVATION

Even if an organization has committed an objectively dishonest act, this does not mean that the “prohibited act” element of the offence of fraud is automatically made out. Also required is proof that the prohibited act has resulted in a deprivation or risk of deprivation to the victim’s economic interests. Notably, actual *economic loss* by a victim is not an essential element of the offence of fraud. All that is required is proof of detriment, prejudice or *risk* of prejudice to the victim’s economic interests. Risk of prejudice can be established upon proof that a complainant has taken some form of economic action that, but for the accused’s dishonest conduct, they would not have otherwise taken. This will be the case even if the action taken by the complainant does not give rise to an actual economic loss or to an increased risk of loss.

THE “CRIMINAL INTENT” REQUIRED FOR FRAUD

To establish liability for fraud, it must also be proven that the prohibited act was committed with the requisite criminal intent. This requires proof that the accused was subjectively aware that they were undertaking a prohibited act (e.g., making a statement knowing it to be false) and was subjectively aware that in carrying out this prohibited act they could cause deprivation by depriving another of property or putting that property at risk. Even if an accused did not intend that a deprivation occur to the victim, it is not relevant to the establishment of the criminal intent for fraud.

Proof of recklessness or wilful blindness is also sufficient to establish the requisite criminal intent for the offence of fraud.

Nevertheless, the standard of subjective fault is high, as the court underlined in *R. v. Duffy* where Senator Mike Duffy was acquitted of fraud, corruption and bribery offences relating to certain expense claims.³ In that decision, the court emphasized the importance of subjective criminal intent, explaining that an individual cannot be coerced or tricked into committing fraud. In acquitting the defendant, the court also noted the absence of so-called “badges of fraud” (such as diversion of funds for personal use, kickbacks sought and/or paid, and secrecy) that can provide evidence of criminal intent.

Actual *economic loss* by a victim is not an essential element of the offence of fraud.

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