

ISSUES FOR LENDERS
A NEW ZEALAND PRACTITIONER'S
PERSPECTIVE

John Greenwood

Partner

Chapman Tripp

Wellington

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INTRODUCTION

The process of moving to electronic registration in the Land Titles System in New Zealand commenced in 1996. Land Information New Zealand (*LINZ*) received Government sanction to fund the build phase of converting paper records by scanning stored records into a computer database system.

The New Zealand Law Society (*NZLS*) appointed a Working Party Committee on automation, which later became the Property Law Section Land Titles Committee. Tim Jones and I were appointed co-convenors of that Committee.

At the end of March 2003 the commencement of Landonline registration started in New Zealand.

Currently the electronic environment will allow 70% of all conveyancing transactions to be processed using e-dealing. Routine discharges of mortgage, transfers and new mortgages (DTM's) are capable of e-dealing. It is anticipated that over the next 12 months or so more transactions will be capable of being captured in the electronic environment such as transmissions and easements.

Under the current New Zealand regime a dual system operates. Practitioners have a choice of continuing to use the manual registration environment or the electronic environment. Within the next two or three years LINZ may cease manual registration and make all land transfer dealings mandatory. Under section 24 of the Land Transfer (Computer Registers and Electronic Lodgement) Amendment Act 2002 the Registrar General of Land can by Order in Council introduce a mandatory process for all dealings.

Currently practitioners also have a choice of whether or not they use both electronic searching and/or e-dealing processes.

Some 7 million historical records have been converted and practitioners are able to access such records electronically. Although the uptake has been slow a number of initiatives over the last few months will undoubtedly see the uptake escalate ahead of mandatory electronic registration in New Zealand. Indeed over the last four months in New Zealand the number of firms on e-dealing has gone from the 80's to over 200.

The key steps involved to carry out e-dealing are as follows:

Request to act and create authority and instruction form

Clients including lenders who wish to have their transaction electronically lodged must give explicit authority to a conveyancing professional (lawyer with a current practising certificate or licensed landbroker).

The A&I form is a template developed by the NZLS and gives the conveyancing professional the necessary authority to change the register. The A&I form also

protects the conveyancing professional from subsequent challenge as to his or her authority to change the Register.

The A&I form authorises the conveyancing professional to sign as if he or she were the owner. Importantly it instructs the conveyancing professional to register the authorised instruments and provides a status document on the proper identification of the client.¹

The rigorous identification of client requirements does add a second layer of comfort to banks who have their own client identification requirements.

Complete dealing screen

The primary contact, who will typically be the Legal Executive, will complete all the required details to set up the e-dealing, similar to preparing an abstract document in the manual environment.

Prepare instruments

Each instruction in the e-dealing is prepared by the relevant party by entering names, registered numbers and priority figures in spaces provided.

¹ Under section 164A of the Land Transfer (Computer Registers and Electronic Lodgement Amendment) Act 2002 the conveyancing professional needs to certify that:

- (a) the relevant parties have authorised the transaction and have the legal capacity to do so;
- (b) reasonable steps have been taken to confirm the identity of those parties;
- (c) specified statutory requirements have been complied with; and
- (d) supporting evidence has been retained.

An example of the certification required taken from the NZLS guidelines on use of Landonline (see www.proplaw@lawyers.org.nz): "I hereby certify that:

- (i) I have witnessed the client (or his/her attorney) sign this form; and
- (ii) I have sighted the original form of identity ticked above; and
- (iii) I confirm that the photo and name match the person who signed the form; and
- (iv) I confirm the person appears to be of sound mind; and
- (v) I have attached either a copy of the form of ID used or details (eg passport number) where copying is not practicable".

Note for proof of identity of corporate lenders it is sufficient for the conveyancing professional to rely on the face of the corporate lender's authority without personally establishing the identity of the individual who signed or authorised e-dealing on behalf of the corporate lender. The conveyancing professional must be satisfied that the authority on the face of it reasonably appears to be from the corporate and if not further inquiry must be made as to the bona fides of the documentation provided.

Certify and sign

This process can only be completed by the conveyancing professional – not the Legal Executive. This is similar to signing a document correct in the manual environment. This process can occur well ahead of settlement arrangements.

Release

Once settlement arrangements have been confirmed as between each party, each instrument is released by the vendor's Legal Executive to indicate that settlement has been completed. This is similar to sending off manual documents or having them handed over at settlement.

Submit

Once all instruments have been released by the purchaser's Legal Executive the e-dealing can be submitted to LINZ for registration. Again the Legal Executive (for the purchaser) will ordinarily complete this task.

Registration

Immediately submission occurs you receive automatic email confirmation of registration and you are able to obtain a search confirming registration.

What are the benefits for lenders?

There are numerous benefits for lenders. In no particular order, I discern these to be as follows:

Speed of delivery

In conveyancing transactions delay has always been the enemy since completion of settlement does not guarantee immediate registration. Indefeasibility is not assured on completing settlement. Electronic conveyancing will bridge the gap and achieve immediate priority. The New Zealand electronic environment contrasts with Ontario and other jurisdictions where, although there is electronic lodgement, it does not mean automatic registration. In other jurisdictions documents lodged electronically are then checked by land registry staff.

Reduce costs

The registration fees are considerably reduced and there are no agency fees. There is also reduced time in producing documents and processing registration. Importantly, the elimination of paper based requirements such as duplicate titles and mortgage and lease documents will reduce paper handling and storage costs.

While initial investment is required in terms of hardware, software, technical expertise and training the medium/long term benefits suggest considerable upside.

Adopting modern technology and relying on less processing staff will improve business efficiency.

No lost document hassles

There is no need to replace missing documents. The time consuming and often frustrating exercise in perfecting lost documents and waiting for public notification periods to expire is no longer a risk.

No doubt those banks and lenders who do their own conveyancing will present an opportunity to save on conveyancing and registration costs. This in turn will present a competitive edge opportunity by savings being passed on to customers.

Standardisation

Automation requires standardisation and will lead to reduced compliance costs in standardising mortgage documentation. If the different states in Australia could adopt a common approach then new and welcome efficiencies should result. This could realistically extend to capture New Zealand. Recent trends in investment on both sides of the Tasman give a lead in suggesting a standardised approach to banking documentation.

Remote access

You need not be located in the local registry to secure registration. Access is obtained through a secure channel over the internet. Thus searching and e-dealing can be achieved whilst on an island holiday.

Risks reduced

These include the following:

- The need to properly identify clients by requiring a copy of a passbook or car licence and/or in addition copies of rate and insurance receipts to cross

check client identity. This mandatory requirement will serve to back up lenders own identification of client requirements and serve to underpin the integrity of the automatic Torrens System.

- The computer based system has a robust in-house checking and verification system so that wrong names or title references are picked up prior to registration automatically.
- Law Society rule changes mean that a breach of rules will occur if a practitioner allows his or her digital certificate or associated password to be used by any other person.²
- There is a transparent audit trail with automation.
- The Registrar-General of Land (*RGL*) carries out routine checks on all transactions. In this way the RGL is still obliged to ensure that electronic instruments are in order for registration. Licensed conveyancers are required to hold supporting evidence for their certifications for ten years and make this available for audit purposes. In worse cases the RGL has the ability to revoke a Conveyancer's Licence.
- Once an electronic instrument is certified and signed the information it contains is effectively locked and secured. If prior to registration the instrument details are altered the certifications are automatically revoked. Once altered an instrument must be resigned and re-certified.³
- The LINZ User Contract provides strict duties on use of the Landonline searching facility and e-dealing
- There is greater interface between Legal Executives and professional conveyancers. In-house rules will be required to ensure proper procedures and signoffs are processed at all points as distinct from the manual conveyancing environment where a lawyer may have no knowledge or understanding of the transaction. This is a quality control aspect that really ought to be mirrored in the manual environment.
- The Digital Certificate requires both a password and pass phrase known only to the holder of the Digital Certificate.

² New Rules 3.03 and 3.04 provide as follows:

3.03 – "A practitioner must take reasonable steps to ensure that any certificate given by that practitioner under section 164A Land Transfer Act 1952 is correct and complies with the statutory requirements".

3.04 – "A practitioner must not allow use of his or her Digital Certificate (DC) or the associate password by any other person".

³ See paper of Robbie Muir, Registrar-General of New Zealand titled "Electronic Registration: The Legislative Scheme and Implications for the Torrens System in New Zealand" in text "Torrens in the Twenty First Century" edited by David Grinlinton being a publication of all papers delivered at Auckland conference on 19-21 March 2003

- There must be some additional comfort knowing that a practitioner and not a Legal Executive has the ultimate signoff responsibility, although the Legal Executive still handles the final settlement and registration process. In any event as with the manual environment what continues to underpin the basic security requirement of the Registry is the trusted professional.
- The New Zealand Law Society guidelines on use provide a further underpinning of quality control in terms of procedures.
- The pre-validation of documents in the computer working space provides a useful tool which can more readily be updated and which will deliver greater accuracy and correct information to the Registry.
- There are reasonably severe penalties under the new automation legislation where incorrect and/or fraudulent certifications arise.⁴
- Rejections will not result and with the delay experienced in the manual registration environment opportunities for caveats or matrimonial property notices to be lodged will present only a remote risk.

Disaster recovery

While Landonline is in operation there is a continuous backup tape running for all dealings entered into the system, whether they are e-dealings or via the paper manual lodgement. This journal together with the daily backup of the system ensures that no more than one day's work should be lost. The continuous journal ensures capture of the details of any dealings that might be destroyed at the time of any disaster occurring.

It is important to draw a distinction between a simple "outage" and a "disaster". An outage is an occurrence where the system for whatever reason (software failure for example) is off-line for a short period of time. A Disaster Recovery Plan may be invoked if the computer system remains down for any prolonged period. Once invoked then it is anticipated by LINZ that it should not be more than 72 hours before recovery is achieved. That plan which is tantamount to a business continuity plan calls for the recreation of the Landonline infrastructure including all conductivity and security elements at an alternative site and the restoration of the database from backup tapes. Currently LINZ are working on enhancing their existing disaster recovery back-up systems.

When Landonline launched last year there were a few outages, which did cause some problems on settlement day, but most of those early teething problems now appear to be over. In recent times outages have become less frequent as new security and backup integrity is improved.

⁴ The RGL has the ability under section 164B(2) of the Land Transfer (Computer Registers and Electronic Lodgement) Amendment Act 2003 to revoke a conveyancing professional's licence. This may occur where a certification is fraudulent or materially incorrect or there has been a failure to produce audit information under section 164C. New criminal offences of knowingly or recklessly giving a false certificate may lead to penalties of up to four years imprisonment or imposition of a fine. In worse cases a practitioner could have their practising certificate revoked by NZLS.

Removal of duplicates

There is no longer any need to deal with lost duplicates. Duplicates in any event were never the definitive title record. That has always been and continues to remain with the original Registry record, not what exists on a duplicate or triplicate copy title document.

Removal of duplicates also removes an opportunity of having duplicates re-produced by a fraudster.

Unlike an electronic system which sees documents stored as images in the paper environment a fraudster could conceivably alter an original paper document without trace.

Ironically removing duplicates removes the temptation to commit fraud since arguably a person in possession of a title would have the appearance of either being the owner or the person empowered to deal with the title. Indeed in many fraud cases innocent parties act instinctively in accepting the fact that the person who holds the title, has legal authority to deal.

Deals with volume

The move to electronic registration will more easily be capable of dealing with large volumes of conveyancing traffic. Instead of relying on a small Land Registry Team, in practical terms the conveyancing professional acts as a de facto Registrar-General of Lands. This will ease the time pressures on Registries to deliver.

Cross selling

Over time it is expected that the Landonline system will integrate with other national and local Government related systems such as planning and rates information. Ultimately there might be one omnibus system as the integrity of the automation processes improve.

Security aspects – The need for conveyancing practice to change

In any electronic environment there is always constant change. While a paper environment can remain stagnant for many decades a blessing of computerisation is the constant demand to make systems more user friendly and at the same time face the demand of introducing quality controls to minimise abuse.

It is inevitable that more robust computer security will be implemented over time. While the existing Landonline security measures and controls are generally considered to be adequate some debate continues around possible enhancements for the future. Also, it must be acknowledged that many of the security aspects are not confined to computerisation but embrace conveyancing practice itself.

Some of the suggestions mooted in New Zealand and overseas include:

Witnessing

- Tightening up the witnessing to reduce cases of fraud and forgery.⁵ In New Zealand any adult person is capable of witnessing. Perhaps reverting to witnessing by solicitors, Justices of the Peace, Commissioners of Oaths and Public Notaries could be entertained. Also, demanding more rigour from the person attesting ought to be considered such as requiring a similar level of proof as for the new client identity rules. Conversely some jurisdictions have abandoned the need for witnessing altogether for particular instruments.

Biometric and Tan identification

- Adopting more robust identification processes such as by having a unique pin identification. The New Zealand Stock Exchange has a twin pin system which adopts a customer number and share transaction number (CSN - Common Shareholder Number) and FIN - FASTER identification number). Bio-metric identification tools available include fingerprint reader, face or voice recognition, retina scan or signature pads. A number of banks already adopt for their own internal audit purposes the TAN (transaction automation number) which gives a bank unique identifiers for each transaction passing through their system.

Escrow settlements

- A move to escrow settlements, which would see document exchange through the electronic environment for no release and submission until all payments were released. In practical terms it could be said that escrow settlements already occur in the electronic environment.

Revert to the Ontario system

- If there are isolated concerns about lawyers taking on the role of the Registrar-General of Lands by being permitted to alter the Register, the alternative compromise approach could be adopted by electronically lodging and having Land Registry staff still approve and register. This however would lead to the same old issues of delay in registration and possible rejection, and not give the certainty or immediacy of registration.

⁵ See Australian cases *Russo v Bendigo Bank Limited* [1999] 3VR376 and *Young v Hoger and others* [2001] QCA 453. It is accepted that fraud by a registered mortgagee includes fraud by its agent. In *Hoger* the solicitor for the lender was accused of fraud where he failed to detect forged mortgage documents. The Court of Appeal concluded that the solicitor did not develop a suspicion of forgery nor was he guilty of actual dishonesty. Thus it seems the threshold of proof is still relatively high.

Strengthen Registrar's powers of correction

- The Registrar's powers of correction in the electronic environment could be improved, rather than reduced. Certainly with the ability now for licensed conveyancers to alter the Registry the need to correct errors may be more compelling. In this regard there would seem to be a good case to expand the Registrar's powers of correction, by specifically allowing the Registrar to amend electronic transactions in certain defined cases. If a Registrar is given additional powers then a control aspect could be the introduction of a robust adjudication process where the parties present their case in an informal setting which may bring about a sense of justice, create greater certainty and ease public concerns about integrity.⁶

Compensate the real victims

- While the compensation provisions in New Zealand continue to apply to electronic transactions more robust compensation provisions should be considered. For example, consideration ought to be given to granting compensation to bona fide lenders if there is fraud. In such a way perhaps the real victims of fraud should be compensated and the Courts and Registrar-General ought to be looking at the competing interests of two innocent parties. That is, the innocent vendor and the bona fide purchaser and/or bona fide lender. In limited cases a bona fide purchaser and a bona fide lender should be rewarded with compensation with the innocent vendors having their property status reinstated. Some principles or guidelines could be established such as:
 - reviewing any suspicious circumstances leading to contracts of sale such as complicity between the parties;
 - introducing a sunset provision, say six to twelve months out, from when a fraud is actually detected;
 - considering the impact of the bona fide purchaser carrying out any improvements;
 - review the emotion and spiritual upheaval for the innocent vendor, such as having an established heritage home sold without their knowledge;
 - consider the disruption to a bona fide purchaser; and:

⁶ See David Grinlinton's paper titled "*The Registrar's Powers of Correction*" at page 217 of where he advocates more clarity as to the extent and manner of the exercise of the Registrar's powers. See also leading New Zealand case *Housing Corporation of New Zealand v Maori Trustee*[1988] 2 NZLR 662, McGeghan J.

- examine all relevant other matters that ought to be going into account to deliver a just and equitable outcome.⁷

Freeze the Registry

Maybe a freeze on the Register, as occurs in the manual environment in England, could occur in the situation where notice is given prior to settlement that a bona fide purchaser and bona fide lender are about to complete settlement.

Simultaneous transfer

Having bank to bank transfers of electronic funding could take place contemporaneously with the electronic registration process and make security components of conveyancing even more robust and secure.

Confine use to experienced persons

Accreditation and compulsory continuing education courses would greatly assist the underpinning of the trusted professional. The existing and former experienced land registry staff can act as a useful resource of captured knowledge. A more conservative approach would be to allow only persons with certain relevant experience to become licensed conveyancers.

More robust audits

More robust audits could be undertaken and penalties increased.

Compulsory PI cover

PI insurance should be compulsory as a condition of instructing a lawyer. This may of course require legislative endorsement.

Should a lawyer act for both parties?

A further conservative approach is that maybe a rule could be introduced that the conveyancing professional or licensed conveyancer should not act for both lender and borrower.

⁷ See author's and Tim Jones' paper titled "*Automation of the Register: Issues impacting on the Integrity of Title*" at page 346 in the text noted in footnote 4. Also see Joint Titles Committee report in Canada in 1990 titled "*Renovating the Foundation: Proposals for a Model Recording and Registration Act for the Provinces and the Territories of Canada*".

Do lenders need external lawyers?

Maybe lenders can more routinely carry out registrations on their own without outside legal counsel assistance. There will be many routine conveyancing transactions that arguably do not require that level of independent professional assessment and advice.

Adopt umbrella licences

Adopting an umbrella licence for organisations since at present licences for use of electronic dealing is limited to individuals.

Speed access to electronic workspace

Reduce the time it takes to access the electronic environment.

Promotion

Adopt a more overt promotional campaign to convince the cynics and luddites that electronic registration works, that it is cost effective and that the integrity of a computer based system is more robust than the manual environment.

Standardisation

Adopt standardisation with regard to mortgage documentation, solicitors certificates and instructions to solicitors, putting to one side the claimed competitive edge issue. Many certificates required by banks defy reality and in nearly all cases ought to be varied by the certifying solicitors.

Template consents and discharges

Adopt templates for mortgagee consents and discharges.

Lenders sort out priority amount problem

Resolve the priority issues in terms of mortgage advances and sums secured. There are broad differences of approach in addressing what future advances and other customer bank accounts can or ought to be capable of being secured under mortgages. Greater transparency and understanding is required by lenders and customers. Reverting to priority

deeds would give customers greater certainty and knowledge rather than placing reliance on unrealistic S80A priority amounts in loan or mortgage documents.⁸

Accept work habit behavioural change

Accept that work habit behaviour needs to adapt to a new way of doing business.

Expand instruments that can be registered electronically

Allow more instruments to be registered electronically to improve the service to the wider community, especially developers of subdivisions.

Prior mortgagee consents

Introduce a regime where no second and third mortgage may be registered without existing mortgagee consent.

Educational tools

Improving wizards or electronic sources of knowledge are critical tools of encouraging uptake. Putting on line Registry rulings, frequently asked questions, computer software tips, checklists on best practice etc will continue to help.

Disaster recovery

Where cost permits having a full backup computer at a different geographical location would serve to remove the occurrence of any prolonged stoppage and diminish any outage downtime which would give added comfort to allowing settlements to proceed on time.

Expand interests registry

To add more transparency and integrity the "interests", that may be noted in the Interest Registry, could be expanded. Great care however would be needed to ensure that only those interests that grant an estate and interests or which otherwise truly impact on an estate

⁸ Section 80A(2) of the New Zealand Property Law Act will defeat the rules in *Hopkinson v Rolt* [1869] 9HLC 514 and in *Claytons* case (1816), mer 572; 35ER 781 by allowing lenders to nominate a maximum amount in excess of the first drawdown on funds, so allowing further advances to be secured to rank ahead in priority to any subsequent mortgage.

in land are noted. The debate over rights enforceable in rem and those only enforceable in personam would need to be faced.

Vendor disclosure

In New Zealand we still do not have any statutory compulsory vendor disclosure requirements other than that recently introduced through the Retirement Villages Act 2003. A move requiring disclosure of all relevant property information prior to signing contracts would serve to underpin the integrity of title to be received and provide a further risk reducing measure to give lenders and purchasers greater comfort.

Standard sale terms

As with vendor disclosure there is no statutory implied terms or conditions imposed on sale of property transactions other than the most basic terms of conveyance set out in the Property Law Act 1952.⁹ Inserting implied statutory terms, such as providing that any unavailability of the electronic Registry, through no fault of the vendor, would not constitute a default even if time were of the essence, would serve to strengthen the integrity required in property transactions.

Title insurance

Title insurance for defects in title is establishing a foothold in New Zealand. Its existence is well documented in the United States. Canada has in recent times been more proactive in adopting the need for title insurance to be taken out. Lenders are driving the need for such insurance cover to be taken out to underpin the State guarantee of title. One can only hope that it does not replace the State guarantee. We will just need to see how it evolves in terms of lender demand, cost effectiveness and the extent to which cover applies once the exclusions of cover are taken into account.

Conclusion

The challenge for lenders is to embrace new security requirements with the technology now available. The new environment following Enron is witnessing a strengthening across international borders of demanding rigour in identification of client requirements and new forms of certifications. The case for the fraudsters is going to get harder. A paper environment offers more risk in my view than the electronic environment where rapid change can result to adapt to any new areas of risk in the future.

⁹ See sections 72 and 73: This Act is currently the subject of another attempt at overhaul following the first attempt last decade which followed the 1994 New Zealand Law Commission Report number 29.