

MANAGING MORTGAGE RISK

AMADIO AND BEYOND FEBRUARY 2010



LEGAL
PRACTITIONERS'
LIABILITY
COMMITTEE

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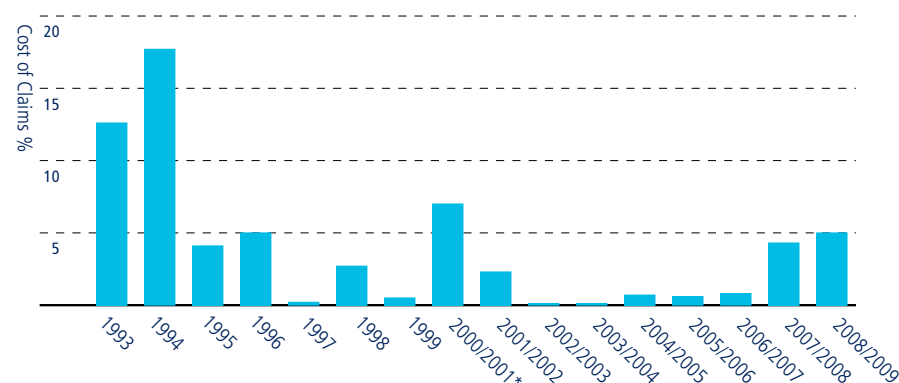
Introduction

When the first edition of this booklet (*Learning from Amadio*) was distributed to solicitors in 1995, the statistics for 'Amadio type claims' were alarming.

Current statistics show that the advice offered in the earlier editions of this booklet has been heeded. Greater awareness of the risks in this area together with the adoption of the LIV ABA solicitor's certificate package led to a dramatic reduction in Amadio claims since their peak in 1994. However, the last few years has seen an increase in these types of claims again. See the graph below.

Given the recent credit crisis there is no room for complacency in this area. New and varied solicitor's certificates are still being produced and solicitors must be on their guard. This booklet gives a summary of the original Amadio case, the first and second waves of Amadio claims and related areas of risk – improvident transactions, mortgage fraud and an area of emerging risk – equity release products. We provide a checklist, copies of the solicitor's certificate package, the related practice note and the relevant professional conduct and practice rules.

Percentage cost of Amadio claims over total cost of claims (as at July 2009)



*2001/2001 was an 18 month policy year

Mortgage fraud

Given the recent rise in mortgage fraud claims, we have introduced a chapter on this subject. We identify the common themes that recur in fraud claims seen at LPLC. This will help you to spot potential fraud before it occurs and prevent you from becoming an unwitting participant in a mortgage fraudster's scheme.

Equity release products

We have also added a chapter on the emerging risk of solicitor's advice on equity release products. Lenders require that a borrower obtain legal independent advice on reverse mortgage products before they proceed. This exposes the solicitor to potential liability when things go wrong. These products are notoriously complex with potentially serious consequences for the client borrower. We provide guidelines on how to discharge your obligations to the client when you are retained to advise on an equity release borrowing.

The adage 'prevention is better than cure' is never more true than in this area of the law. We trust this booklet remains a valuable resource for solicitors.

Refresher: Commercial Bank of Australia -v- Amadio and Anor [1983] HCA 14; (1983) 151 CLR 447

In this landmark case impacting on the involvement of solicitors in lending transactions, the High Court held that a mortgage and guarantee provided by Mr and Mrs Amadio to support an overdraft facility to their son's building company should be set aside.

This was in light of the bank's unconscionable conduct in obtaining execution of the mortgage and guarantee when it should have been evident that the couple was under a special disability, namely:

- their age and limited English;
- their reliance on their son in business matters; without the benefit of independent advice;
- the circumstances in which the documents were signed.

As a result of the *Amadio* case and others which followed, the need for security providers (including surety mortgagors, guarantors and direct borrowers) to receive independent legal advice in lending transactions has become a regular part of lending procedure in Victoria.

Lenders now commonly stipulate that security providers must receive independent legal advice from a solicitor before signing the documents and that the solicitor must sign a certificate confirming the advice has been given.

A large number of solicitors have been sued by both security providers and lenders in respect of the advice given or the lack of it.

Such claims are known as *Amadio* claims.

Two types of Amadio claims

Type 1: Solicitor's certificate claims

The solicitor has been asked to provide a solicitor's certificate to the effect that the documentation relating to the transaction has been explained to the security provider. This advice is then disputed.

For example, it is alleged:

- the solicitor did not adequately explain the extent of the monetary obligation to be undertaken by the security provider; or
- the solicitor did not adequately explain that enforcement against the security provider might force the sale of the security provider's home and financial destitution.

Type 2: Unrepresented security providers

The solicitor believes that he or she never acted for the security provider, only for the borrower (or, in some cases, the lender). This is not the view of the security provider who argues that some kind of retainer existed or duty was owed and that the solicitor failed to protect his or her interests. In those cases the security provider may also allege that the solicitor had a conflict of interest.

Chapter one: Amadio claims

Solicitor's certificate claims

A solicitor's certificate in any transaction necessarily increases the risk of a claim being made against you because it positions you for liability if the security provider is able to challenge the content of the certificate.

Claims experience shows that providing solicitor's certificates can be risky business.

Some practitioners and firms refuse to provide certificates other than to existing clients because they regard the risk as too high. Other firms have a policy that only one person in the office is authorised to provide solicitor's certificates. This controls the types of clients for whom certificates are given and the quality of advice provided.

The claims experience reveals two high-risk categories.

New clients

This covers people who are not existing clients of the firm, particularly clients who 'walk in off the street' and referrals from relatives or a bank, finance broker, agent or other third party. A problem we typically encounter is that the solicitor treats the attendance as a request for mere witnessing of documents, rather than an occasion calling for the provision of professional advice, and as a result fails to follow the LPLC recommended procedures detailed on pages 6-9 of this booklet.

Third party security providers

The second high-risk category is guarantors or third party mortgagors in a transaction where the practitioner or firm is also acting for the borrower. The practitioner often fails to appreciate the security provider's different interest to the borrower and the prohibition in Rule 8.6 of the Professional Conduct and Practice Rules reproduced in Appendix Three on page 42 of this booklet.

Firms are encouraged to develop criteria for when they will provide solicitor's certificates and to create a protocol based on the following recommended procedure.

LPLC recommended procedure

WE RECOMMEND:

Ask for identification and record the evidence produced.

Fraud is increasingly common and title deeds can fall into the wrong hands. We have seen cases where the person introduced as the borrower's nearest and dearest is actually the borrower's partner in crime. Asking for identification need not be embarrassing or offensive. It is just a sound principle of doing business. Keep a copy of the identification provided.

If a client has limited English, use an independent interpreter.

This will protect you from any later allegation by clients not conversant in English that the transaction was not properly explained because you spoke in English. You should obtain a form of confirmation from the interpreter that your explanation and the client's statements were translated before the documents were signed.

If you speak the client's language then, of course, you do not need an interpreter but you may be asked to verify your proficiency if the certificate is ever challenged.

Under no circumstances should you use the borrower as an interpreter when you are advising a security provider, no matter how obliging the borrower may be. Remember, you are providing independent legal advice and the borrower will not be seen to be independent. It is in the borrower's interests, for example, for the implications of the mortgage to be toned down in order to persuade the security provider to sign on the dotted line.

We have seen a number of cases where security providers allege that they only signed the documents as a result of the misrepresentation by an interested party of which the solicitor should have been aware. Borrowers should never be present while you advise the security provider. If they do accompany the security provider to your office they should remain in the reception area.

If there is more than one security provider, advise each separately as to their obligations.

The security providers' interests may not be the same. For example, one may have more assets at risk than the other. Consider whether there is a conflict of interest that prevents you from advising more than one of the security providers.

When advising a surety mortgagor or guarantor be sure to do so independently of the borrower who may often accompany them.

We have seen cases where clients have alleged the solicitors ought to have been aware that they signed the document under pressure from an interested party. You should take steps to satisfy yourself that there is no question of undue pressure or duress, particularly in those cases where the borrower is receiving the benefit and the security provider is taking all the risk.

Always ask why the security provider wishes to become a party to the transaction and record the answer.

Enquiring as to why the security provider wants to enter into the transaction is important because it will reveal the 'danger cases'. These are the cases in which the borrower is receiving the benefit and the security provider is taking the risk.

If you suspect that there might be undue influence or duress, you should advise the security provider not to enter into the transaction. If you still suspect either or both of these situations and the client wishes to proceed, you must not provide the certificate.

WE RECOMMEND *continued*:

☑ **Make it clear to the client that you are not providing financial advice.**

Recommend that your client seek **independent financial advice** before signing the documents, if this is required. If you think the client has unrealistic expectations of the outcome of the transaction, you should insist that they obtain independent financial advice before proceeding and allow them time to do so before signing the documents.

☑ **Never give a certificate in respect of a pre-signed document.**

This amounts to false witnessing of a document. Unless you have witnessed the signing of the document you cannot certify as to execution by the client.

☑ **Keep proper records of the advice you have given the client.**

Open a file, make a file note and confirm your advice to the client in writing. If you obtain a written acknowledgment of the explanation you have provided and that the client understood your explanation, you should still keep a file note of what occurred at the meeting. We have claims where the client denies receiving the advice set out in the acknowledgement and a file note goes a long way to countering this.

You should also consider video or audio taping the meeting with the client where the advice is given. A copy can be given to the client and one kept for your file. We have seen a case where the production of such a tape expedited the release of the firm from an *Amadio* claim.

It is important to remember that the advice you know you gave may later be denied or disputed. You can substantially protect yourself by keeping **good written records** of the conference you had with the client before signing the solicitor's certificate.

☑ **Make sure your advice is complete.**

It is important to explain to clients in the simplest language possible important issues such as:

- joint and several liability;
- that the mortgagors could lose their homes; and
- that the amount the security covers can be more than the amount borrowed.

The client needs to understand the general nature and effect of the documents and what could happen in the worst case scenario. Asking your client at the end of your explanation what he or she understands to be the position and recording such responses is one way of ascertaining the degree of understanding. It is not sufficient evidence of understanding for the client to just nod and say 'yes, I understand'. The client needs to articulate what he or she understands.

☑ **Charge appropriate fees.**

When providing a solicitor's certificate it is recommended that you charge a fee which reflects the risk as well as covers the necessary steps and precautions. The fee, it could be pointed out, will still be less than the loan establishment fee paid to the bank.

The LIV ABA solicitor's certificate package

A recommended form and procedure for use by solicitors and lenders was published in the October 1994 edition of the Law Institute Journal. The 'solicitor's certificate package' comprised: two solicitor's certificates, an interpreter's certificate and a form of client acknowledgement. A practice note was used to implement the new forms. The solicitor's certificate package was approved by both the Law Institute of Victoria Council and the Australian Bankers Association (ABA) in 1994. All ABA members operating in retail banking in Victoria agreed to participate in the use of the package at that time. The LPLC had considerable input into the solicitor's certificate package and it incorporates much of the recommended LPLC procedure. The certificates remain in use today.

It appears some banks and financial institutions currently produce their own form of certificate, but if pressed, will usually accept the LIV ABA form of certificate. You should insist on using the LIV ABA form of certificate where ever possible.

The most current versions of the certificates (the solicitor's certificates are now entitled 'Australian Legal Practitioner's Certificates 1 & 2') and the acknowledgement and interpreter's certificate are reproduced as Appendix One. The practice note is reproduced as Appendix Two.

The certificates and acknowledgement can be purchased from the Law Institute of Victoria bookshop or online at www.bookshop.liv.asn.au. (The bookshop item codes are 3.1 – 3.4.)

The two forms of certificates are designed to cover two categories of clients:

- Australian Legal Practitioner's Certificate 1 –
where the client is the direct borrower or is a security provider referred to in the documents as the borrower.
- Australian Legal Practitioner's Certificate 2 –
where the client is a third party guarantor, surety mortgagor or indemnifier for the principal borrower.

WE RECOMMEND:

- ☑ You use LIV ABA solicitor's certificates even if another form of certificate is provided for signature by your client's bank or financier. You should press strongly for their use as the recognised and approved forms in Victoria.
- ☑ If you are faced with a difficult lender who refuses to accept a solicitor's certificate in the LIV ABA approved form, you should:
 - still use the client form of acknowledgment and interpreter's certificate (where appropriate); and
 - try to incorporate amendments on the basis you are only certifying that you have explained the **general nature and effect** of the documents to the client and that the client **appeared to understand**.

Client expectations

The solicitor's certificate package does not solve all the problems associated with Amadio claims. One of the reasons for this is the tendency of lenders to tell their customers that their security documents need to be signed 'in front of a solicitor' rather than that they need to seek legal advice before signing the documents. That is, the emphasis is often on obtaining the signature rather than obtaining the advice.

The trouble with this approach is that it primes clients to expect that the process of obtaining a solicitor's certificate is akin to having a passport application witnessed. This expectation can lead to clients becoming dissatisfied by the procedures and costs involved.

In response to the LPLC's concerns, the Australian Bankers Association (ABA), at the time the solicitor's certificate package was launched, encouraged a branch level education program about the legal service value of the certification process. In particular, the program included instructions that bank officers should:

- not advise customers to come back 'in five minutes' with a signed solicitor's certificate;
- explain to customers that it is the bank's requirement that a solicitor's certificate be obtained;
- explain to customers that legal advice is required, not merely the witnessing of documents; and
- advise customers that the solicitor will need to consider the documents before providing the legal advice and be entitled to charge a reasonable fee for the service.

The ABA has, in more recent times, created a *Banking Code of Practice* which covers a wide variety of issues but, in particular, prescribes the information that banks should give to guarantors before they accept guarantees from them. This information includes telling the guarantor that he or she should obtain independent legal advice as well as giving the guarantor information about the credit facility that is to be guaranteed and the creditworthiness of the debtor. A copy of the Banking Code of Practice, as well as a list of the banks that have agreed to comply with it, is available on the ABA website at www.bankers.asn.au.

New and inappropriate forms of certification

Initially it appeared that the solicitor's certificate package was widely accepted and used, but new and inappropriate forms of certification are always emerging. Some banks, financial institutions and franchisors have deviated from the approved forms and some forms purport to certify matters other than explanations of mortgages or guarantees.

EXAMPLES:

Certificates with misleading headings

In some cases a certificate headed 'Certificate of witness/identification' not only asked for certification that the signatory was one and the same person as that named in the mortgage but also asked for certification that the signatory had signed the mortgage of his or her own free will and with full understanding of the documents. This document was, by stealth, a solicitor's certificate. Always read the document before signing it and do not rely only on the heading.

Inappropriate warranties

We have seen certificates where the borrower's solicitor was asked to certify that the loan documentation was enforceable against the borrower. Another form of certificate stated that 'the solicitor will warrant the warranties provided by the guarantor'. Neither of these certificates or warranties are appropriate for a solicitor to give when acting for the borrower or guarantor.

A 'trust opinion certificate' required the solicitor to warrant that the trust documents given to the solicitor contained all the terms of the trust, that there was no conflict of interest which would preclude the trustee entering into the loan, and that the loan was for the benefit of the trust. All matters which, without significant qualification, the solicitor should not warrant.

Certificates that are too broad

A certificate entitled 'Certificate of Independent Legal Advice' recently referred to us looked a lot like the LIV ABA certificate however it required the solicitor to certify broadly that the solicitor had 'advised the borrower before any of the documents were signed'. There was no further detail about what the advice covered.

The document also contained a statement that: 'This certificate cannot be relied upon unless it is in the exact form prescribed by the Law Society of NSW without alteration and ... is given by the holder of a current practising certificate...'. This gave the impression that the document had the imprimatur of the Law Society of NSW which it most certainly did not. Eventually the lender in question was persuaded to accept the LIV ABA form of solicitor's certificate instead.

Certificates that relate to financial advice

A certificate referred to us by a solicitor required an independent financial adviser to advise the client about the financial impact and effect of the loan. The loan was one that capitalised the interest. Much of the certificate referred to financial advice and there were also aspects of the certificate that appeared to require legal advice. When the bank was asked as to whether a solicitor was required to sign the document the bank indicated that 'many solicitors' had in fact signed such certificates. For this style of loan, the bank did not require a separate solicitor's certificate. While it was clear that clients seeking to enter into these types of transactions required legal advice, it was equally clear that the type of certificate provided by the bank went beyond the realm of legal advice and was not one that a solicitor should be signing.

Franchise certificates

We have seen many and varied solicitors certificates relating to the purchase of a franchise. There is no standard form. Solicitors should read these certificates carefully and not sign a certificate that states the solicitor advised the franchisee and the guarantor unless they are the same person.

Solicitors should never be complacent about the content and form of solicitor's certificates. Scrutinise what you are being asked to sign. Consider whether the certificate proffered is appropriate and reasonable. Ask yourself whether you can personally vouch for the contents of the certificate. Do not sign unless the matters contained in the certificate are within your knowledge and true.

Unrepresented security providers

The second category of *Amadio* claims involves solicitors acting for borrowers or, occasionally, for lenders where solicitors have assumed that the security provider in the transaction is unrepresented. Typically this assumption is challenged by a writ alleging the solicitor acted for the security provider in a conflict of interest.

Transactions involving security providers always require caution – especially where these parties are unrepresented. Experience suggests that it is, above all, these parties who are inclined to argue that they would not have signed the document had they been properly advised.

We still see cases where a solicitor, sued by a security provider claiming a retainer existed or duty was owed, steadfastly maintains that he or she was only acting on behalf of the borrower. However, the manner in which the solicitor conducted the matter sometimes leaves the way open to contrary interpretation.

The recommendations that follow should help you to avoid giving any impression that you are acting for parties other than the ones you intended to act for.

Remember, it is easy for an unrepresented security provider to interpret contact from any solicitor as being the solicitor acting for him or her.

You must ensure that your conduct does not encourage a security provider to labour under this misapprehension because, under the terms of your professional indemnity insurance policy, you will incur a deterrent excess if you acted for more than one party to a transaction or if you breach any professional conduct rules. Rule 8.6 of the Victorian Lawyers RPA Ltd Professional Conduct and Practice Rules 2005 prohibits acting for both borrower and 'guarantor' (defined as guarantor, indemnifier, surety or a person or company providing security for the loan) or both lender and 'guarantor'.

Rule 8.6 is reproduced as Appendix Three to this booklet.

WE RECOMMEND:

- ☑ **To avoid possible legal action when acting for a borrower in a transaction with an unrepresented security provider:**
 - Write to the security provider direct. Enclose the necessary documents and confirm that you are not acting for the security provider and that the security provider will need to obtain independent legal advice. Ask the security provider to return a signed duplicate copy of your letter confirming receipt.
 - Do not answer requisitions on behalf of a security provider under the misapprehension that you are helping to progress the transaction on behalf of the borrower. This only serves to blur the distinction between whom you are acting for and whom you are not. Send the requisitions to the security provider direct with the other documents you sent out initially.
 - Never use the borrower as an intermediary of any description to reach the security provider whether as an interpreter, courier of documents or in any other capacity. The borrower has a vested interest in the transaction and has no legitimate role as an agent.
 - Ensure that the disbursement order is signed by the security provider if the funds are to be disbursed to the borrower. Ensure that the bill is addressed to the borrower - not the security provider. Make sure your file properly reflects who your client is.
 - Be clear in your correspondence with the lender's solicitor that you are acting on behalf of the borrower and not the security provider. You should write 'We act on behalf of the borrower' not 'We act in the above matter'.
- ☑ **When acting for the lender in a transaction with an unrepresented security provider, we recommend:**
 - Do not leave it to the borrower to advise or obtain the security provider's signature as this could set up an argument that the borrower was an agent for the lender who was a party to the unconscionable conduct, so the mortgage should be set aside; and
 - Write to the security provider direct. Make it clear that you are only acting for the lender and not for him or her, so that it cannot be later alleged that you failed to give proper advice.

Recent claims – what still goes wrong?

While the *Amadio* style claims have accounted for a low percentage in both number and cost in the years 2001 to 2006 they never disappeared altogether and are now on the rise again. Solicitors are still being caught out.

Lack of useable trail

Some solicitors still fail to open a file or if they do open a file they do not keep any or proper file notes of the attendance and advice given and the client's responses. They also fail to follow up the attendance with a letter confirming the advice.

Some practitioners keep any notes or letters relating to solicitors certificates on a 'general file' rather than opening a new client file for each matter. This makes it difficult to track down the documents, in the event of a claim, especially if the practitioner is unavailable for any reason or has left the firm or if the advice was given a long time ago and the practitioner can no longer locate the documents.

Word against word

In some cases, although the clients signed an acknowledgment of having received advice, they subsequently allege that they were given no (or incomprehensible) advice about what was complex documentation in a meeting lasting only 10 minutes. The solicitor claims to have given detailed advice in lengthy meetings. Some solicitors justify their lack of file notes by saying they have a standard procedure that they always adopt when giving advice of this kind. The problem with this is that when a claim is made, the issue is one of credit that can only be tested at trial. File notes and correspondence will go a long way to convincing the other side that they have no case, long before the matter reaches trial and may avoid a claim being made in the first place.

Informal retainers

Another circumstance where solicitors tend not to keep a paper trail is when the advice is given at the client's home, often in the evenings or on weekends. You must remember to follow through with the paperwork even when the surroundings are informal.

Claims prevention

The failure to keep a file note is not, of itself, negligent or evidence of negligence but it may leave you exposed to a potential claim by a desperate client. The client and the solicitor's recollections of events and advice given are often very different. Without written file notes or letters confirming the advice, the case becomes a question of who will be believed in the witness box. The existence of file notes often prevents proceedings being issued and on the occasions when they are issued gives us ample opportunity to resolve the matter quickly and cheaply.

WE RECOMMEND YOUR FILE NOTES INCLUDE:

- ☑ the date of the meeting;
- ☑ the author of the file note;
- ☑ details of who was in the meeting;
- ☑ the duration of the meeting;
- ☑ the substance of your advice; and
- ☑ the client's response to your advice.

Allegations of conflict of interest

Third party guarantors

In several recent claims, solicitors gave advice to the third party guarantors and duly executed solicitor's certificates. The allegations were then made that the solicitor either acted for the borrower in the same transaction or had acted for the borrower in other transactions and therefore had a conflict of interest. The cases in this area suggest that the courts will subjectively weigh each case on its merits to determine if the advice given by the solicitor was adequate to alert the guarantor to any relevant risks.

Conflict will be just one of the issues to be looked at. The existence of the conflict seems, however, to make the possibility of a claim more likely, even if the solicitor is ultimately not liable.

Co-guarantors

Conflict can also occur when acting for co-guarantors. Caution is advised in the common scenario where the solicitor is asked to advise co-guarantors with different interests. These are typically husband and wife directors or a de facto couple where one may have more assets at risk than the other. Instructions need to be taken separately from all co-guarantors to ensure their understanding of a transaction.

Chapter Two: Improvident transactions

Many recent cases have considered whether solicitors should have advised their clients against proceeding with various loans because the intended investment was improvident.

The case of Riz

In 2009, the New South Wales Court of Appeal decision of *Dominic v Riz* [2009] NSWCA 216 softened the obligations on solicitors to advise clients about self-evidently absurd or improvident transactions.

The case concerned Mr and Mrs Riz, who intended refinancing their home to invest in a high risk scheme and expected to receive a return on the investment that was described at first instances as 'absurd'. The trial judge held that although the retainer was to advise and act on the loan and mortgage transaction, the duty of care extended beyond the limits of the retainer where the subsequent transaction was so improvident and risky. The trial judge found the solicitor liable but the Court of Appeal reversed this decision.

Prior to the appeal being decided, other decisions explored the scope of the duty of care and whether it may extend beyond the scope of the retainer to include advice on the commercial wisdom of entering a transaction¹. The courts have not been inclined to impose a duty in circumstances where the solicitor did not assume responsibility to the client or there was no reliance by the client.

¹ *David v David* [2009] NSWSC 8, *Kowalczyk v Accom Finance* [2008] 343, *Spiteri v Roccisano* [2009] VSC 132; *Permanent Custodians v King* (2009) NSWCA 600

Riz on appeal

In *Dominic v Riz* [2009] NSWCA 216, the Court of Appeal said the trial judge had gone too far in finding that solicitors explaining loan and mortgage documents are obliged to address the fairness and reasonableness of the underlying transaction. The Court noted that the circumstances in which solicitors have a responsibility to act outside the retainer are 'less than clear'. It acknowledged that if a solicitor sees something outside the retainer that could adversely affect the client then the solicitor may be obliged to inform the client about it.

The Court of Appeal found that the solicitor had given the clients clear advice that they needed to obtain independent legal and accounting advice about the investment they were proposing. The solicitor was found to know nothing about the investment other than that the expected return was very high. The clients were found to be aware of the risks involved.

Risk management

It is good risk management in mortgage and loan transactions to specify:

- the scope of your retainer;
- that you are not giving financial advice; and
- that the client should obtain their own financial advice.

This may not provide complete protection in the event that the client enters into a blatantly improvident transaction. The Victorian Supreme Court in *Spiteri v Roccisano* acknowledged that 'in some cases there may be no bright line of distinction between legal and commercial advice where a solicitor is acting for a client in a commercial transaction'. There is often a blurry line between what is financial and what is legal advice.

While it may be tempting to operate on the basis that the less known and asked about the client's arrangements the better, the risk is that a court may say you should have known or been suspicious or made further enquiries. To avoid that risk it is better to be proactive – you need to know enough about what the client is doing to determine if the matter is clearly improvident, absurd or 'too good to be true'.

WE RECOMMEND

- ☑ Ask your client questions such as:
 - Why are they entering into this transaction?
 - What are they planning to do with the money they are borrowing? What do they hope to gain?
 - If they are investing the money, what sort of investment is it? Is it a managed investment scheme?
 - If it is not a managed investment scheme, does the client know what safeguards there are? What security is offered? What is that security worth?
- ☑ If it is clear that the client needs to get independent financial advice, then you need to forcefully bring that home to the client and give them the opportunity to obtain that advice before proceeding. If your client elects not to obtain independent financial advice consider having them sign an acknowledgement that:
 - they were advised to do so;
 - that they declined to do so for the following reasons – set out what the client tells you about their reasons; and
 - that they are acting contrary to your recommendations in that regard.

Chapter Three: Mortgage fraud

In recent years, we have seen a fairly dramatic rise in number and cost of mortgage fraud claims. Typically, the fraud is committed by a family member upon elderly parents or a spouse.

Here is a shortlist of the signature features of many mortgage fraud claims. If any of these features are present, take the extra measures necessary to satisfy yourself that the borrowing is bona fide.

Signature features of mortgage fraud

- It's a family affair:
 - » adult child defrauds elderly parents; or
 - » one spouse against another.
- Lost or missing duplicate certificate of title.
- Excuses concerning the unseen borrower.
- No photo identification produced by the borrower.
- Certification is being provided to a new client.
- Urgency.
- Settlement money is going to a third party.
- Errors and omissions in the details:
 - » spelling mistakes in names or use of anglicised names different to the names on identity documents;
 - » omissions or incomplete detail;
 - » inconsistencies in forms of signature.
- High risk lender and unencumbered title.
- A third party is actively involved:
 - » non-borrower providing instructions; or
 - » broker.

Incomplete certification

Negligent certifications by solicitors can have the unfortunate effect of facilitating a fraud.

EXAMPLE:

A solicitor was an acquaintance of a young woman who rushed into his office requesting a solicitor's certificate for her parents. The settlement was scheduled the next day and she told him that a conveyancing company was acting for them. The solicitor explained the parents would need to attend the office. Later that day, she returned, pleading with the solicitor and explaining that it was a financial emergency for her parents; her mother was very sick and downstairs in the car. The solicitor attended the parents briefly in the car, verifying the mother's identity by a copy of her driver's licence, but the father produced no photo ID. The certificate signed by the solicitor contained no photo identification of the father.

In fact, the man in the car had been posing as the woman's father. When a claim surfaced, it appeared that the mother and daughter had colluded in the fraud.

Acting for borrowers

WE RECOMMEND:

- ☑ Talk to each borrower directly.
- ☑ Do not take instructions from third parties.
- ☑ Have a good look at the mortgage and loan documents.
- ☑ Use the LIV ABA approved form of certificate (referred to in Chapter One and Appendix One)
- ☑ Insist on photo identification and make photocopies for your records.
- ☑ Never provide a solicitor's certificate in relation to pre-signed documents.
- ☑ Ensure you have a signed authority from all borrowers where money is payable to third parties.
- ☑ Keep proper records of your advice.

Missing certificate of title

Mortgage fraud is becoming more sophisticated. In one case the perpetrator even took the trouble to forge a solicitor's signature on a certificate. Lenders' solicitors need to be alert to this possibility, particularly where suspicions are already raised. A lender's solicitor may be exposed to liability by relying on a flawed certificate or advising a client to proceed in the absence of a title.

EXAMPLE:

A solicitor was acting for the lender and a conveyancing company was acting for the elderly borrowers who were mortgaging the family home. The lender's solicitor was concerned that the certificate of title was missing but the conveyancing company made assurances that an application for a replacement was in progress. The lender himself was keen to proceed and said he would be satisfied with an undertaking about the replacement certificate of title. The lender's solicitor posted the paperwork directly to the borrowers. And although he received the solicitor's certificates, he did not scrutinise them closely.

In fact, the daughter of the borrowers had engineered the entire transaction without her parents' knowledge. The title was not missing; she pretended that an application for a replacement had been made. She had been providing the conveyancing company with the day-to-day instructions, had intercepted mail from the lender's solicitor addressed to her parents and produced forged solicitor's certificates.

Acting for lenders

WE RECOMMEND

- ☑ Confirm with the lender in writing that you are not providing any advice on the financial wisdom of entering the transaction. Tell the lender to make its own enquiries about the borrower's credit history and capacity to repay.
- ☑ Have a good look at the signed solicitor's certificate: check that the details and names are complete, consistent with other transactional documents and that photo identification was provided.
- ☑ If you do not know the certifying solicitor, you can confirm their existence on the Legal Services Board's website at www.lsb.vic.gov.au
- ☑ If any signature features of mortgage fraud appear from page 23 of this booklet, make the extra enquiries necessary to satisfy yourself that this is a bona fide borrowing.
- ☑ Where a lost title application is on foot, do not settle until a new title has been issued.

Chapter Four: Advice on equity release products

The two major equity release products commercially available in Australia today are reverse mortgages and home reversion schemes.

These products pose a range of complex issues and risks for solicitors. There are some important variables to consider in assessing the effect of an equity release transaction: the loan amount, rate of interest and the borrower's life expectancy. Typically, these products involve no repayments and capitalised interest. Equity is eroded very quickly and they are more expensive than traditional forms of borrowing. There is an inevitable measure of uncertainty about the size of the ultimate debt.

As with other forms of mortgage, lenders require borrowers to obtain independent legal advice about the transaction before proceeding. In turn, solicitors may be asked to certify that the borrower has received independent advice about the nature and effect of the transaction.

Before you advise and certify

The client should discuss product alternatives with an independent financial advisor and choose one on the strength of financial advice (including Centrelink and tax issues) before you provide legal advice. There are no 'standard' products or conditions, so before dispensing legal advice you need to spend time reading the fine print. You need to understand the mechanics of the transaction: when the title changes hands, what security the borrower has and particularly, the range of default provisions.

Why equity release?

Understand the context of the proposed borrowing. Remember that equity release products are a more expensive form of finance than conventional loans. They should be understood as a choice of last resort.

Explain the nature and the effect of the transaction and its risks clearly to the client and document your advice. Record why the client wants to use this product and what they understand of the transaction and the risks. Some situations might require you to take extra precautions, for example where the borrowing is for the benefit of a third party or intended as a gift. Act very cautiously where the client appears vulnerable to the influence of another party, the documents are being signed under a power of attorney, English is not the client's first language or there is undue haste to complete the transaction. Decline to act if you consider the client is acting under duress.

Your retainer

Charge an appropriate fee for your advice. Providing the certification for a borrower is more than a simple witnessing procedure. The process will take time and judgement. Be clear that you are providing legal not financial advice. Use an appropriate form of certificate, preferably an LIV ABA approved form in Appendix One.

WE RECOMMEND

- Encourage the client to get advice from an independent financial advisor in order to choose an appropriate product.
- Identify who at the firm is appropriately qualified to advise on these transactions and do not allow others to dabble in this field.
- Develop a protocol for handling these matters based on the following checklist.

LPLC Checklist: Advice on equity release products

While the following checklist is not exhaustive, it is designed to prompt you to consider the many dimensions of these transactions. The checklist may be photocopied for ongoing use.

CLIENT

MATTER

Taking instructions

Explore with the client:

- Did the client obtain financial advice before seeing you? If not, recommend the client seeks financial advice first.
- Have other alternatives been considered?
- What is the money for?
- Who is the money intended to benefit?
- Are family members or heirs aware of the proposed borrowing?
- Does anyone live at the property who is not on title, but whose rights might be adversely affected by the transaction?
- How long does the client envisage remaining in the family home?
- Are there any health issues likely to affect the client's plan to remain at home?
- If the client intends to retire to a nursing home or facility where an aged care accommodation bond is required, will there be sufficient equity left to achieve this?
- Does the client currently receive any Centrelink or Department of Veterans Affairs' entitlements which might be affected by receipt of a lump sum or annuity?
- Is there more than one borrower? If so, see them separately.

The effect of the transaction

Explain to the client:

- When title passes to the lender.
- The basic rights and obligations of the client.
- Whether there is a 'no negative equity' guarantee (and recommend that the client finds a product with such a guarantee).
- If the product creates a life tenancy, the need to protect this by caveat over the property.
- Where the client loses legal title to the property, the need to protect the client's interest by caveat over the property.
- The general nature and effect of the mortgage securing the loan.
- The circumstances when repayment would be required.
- The client's various obligations to ensure a default is not triggered.
- The upfront costs and interest payable. (If the product is a reverse mortgage, give the client the compound interest payable for say 5, 10 and 15 years.)
- What protections there are to remain in the home.
- The consequences if the property is vacated for any length of time.
- In what circumstances the property can be sold.
- When the loan is repayable.
- How the agreement assigns rights and obligations regarding maintenance and insurance, including:
 - who is responsible for payment of building insurance, rates and taxes;
 - any requirement to maintain upkeep of the property in order to avoid triggering default provisions; and
 - details of any powers conferred on the lender to order repairs.
- What constitutes a default and the consequences including default provisions that nullify the 'no negative equity' guarantee.

Issues of duress

Consider:

- Is the money for a third party?
- Are there any indications of pressure from other parties of family members?
- Is the client mentally or physically infirm?
- Does the client have decision-making capacity?
- Is the client dependant on family members to look after his or her financial affairs?
- Are any documents being signed pursuant to a power of attorney?
- Are there communication difficulties because the client's first language is not English?
- Is there family division, particularly between the client's adult children?
- Is the client in an inexplicable rush to complete the transaction?

Generally

- Make comprehensive file notes of the client's instructions and your advice, including the reasoning process, your client's response and duration of the meeting.
- Confirm your advice to the client in writing.
- Use the LIV ABA approved form of certificate.
- Charge an appropriate fee.
- Keep your file.

LPLC Amadio Checklist

While the following checklist is not exhaustive, it does draw attention to the key areas that many solicitors overlook in *Amadio* transactions.

The checklist may be photocopied for ongoing use

CLIENT

MATTER

In relation to solicitor's certificates:

- Allocate just one person in the office to provide solicitor's certificates.
- Open a file in the client's name.
- Use the solicitor's certificate package wherever possible.
- Insist upon identification. Keep copies of the identification documentation.
- Use an independent interpreter when appropriate.
- If there is more than one security provider, consider whether their interests are the same. Does one need to obtain independent advice or will advising them separately be sufficient?
- Advise any security provider independently of the borrower.
- Address the possibility of undue influence or duress.
- Do not provide financial advice - refer your client to a qualified accountant or financial adviser. Ensure they have enough time to obtain this advice.
- Advise the client about the key elements of the documents and the worst case scenario.
- Ask the client why they are entering into the transaction and record the answer.

- Make a comprehensive file note of all attendances on your client, whether in your office or elsewhere.
- Check that your file notes:
 - are dated;
 - identify the author;
 - record the duration of the attendance;
 - record who was present or on the telephone;
 - are legible to you and someone else;
 - record the substance of the advice given and the client's response/instructions; and
 - are a note to the file rather than a note to yourself.
- Confirm your advice in writing and seek a signed acknowledgment from the client.


In relation to unrepresented surety mortgagors or guarantors:

- Advise any security providers in writing that you are not acting for them and that they should seek independent legal advice.
- Do not prepare answers to requisitions on the security provider's behalf.
- Never use the borrower as an agent to reach the security provider.
- Ensure that the security provider signs the disbursement order and that you bill the borrower direct.
- Be clear about who you are acting for in your correspondence with the other side.

Appendix One

Australian Legal Practitioner's Certificate 1

(Schedule 1)
February 2006



FOR USE IN CERTIFICATION WHERE THE PERSON(S) SIGNING IS THE DIRECT BORROWER FROM THE LENDER OR A SECURITY PROVIDER REFERRED TO IN THE DOCUMENTS AS THE BORROWER

AUSTRALIAN LEGAL PRACTITIONER'S CERTIFICATE 1

PART A TO:

THIS CERTIFICATE IS PROVIDED BY:

An Australian legal practitioner holding a current practising certificate under the Legal Profession Act 2004 and not acting for you in this transaction

I HAVE BEEN ASKED TO INTERVIEW:

(called "the borrower")

I HAVE BEEN PROVIDED WITH THE FOLLOWING DOCUMENTS:

(1)

(2)

(3)

(4)

(5)

(6)

PART B EXPLANATIONS GIVEN BY THE AUSTRALIAN LEGAL PRACTITIONER

I explained to the borrower, before the borrower signed the documents, the general nature and effect of the documents required to be signed by the borrower including the risk of loss of any security property and other assets owned by the borrower.

PART C EXCLUDED EXPLANATIONS

I INFORMED the borrower in very clear terms that I was not expressing any opinion nor advising on:

- the viability of the transaction; and
- the borrower's ability to make the required payments to you.

I FURTHER INFORMED the borrower that if in any doubt on those aspects the borrower should obtain independent financial advice before signing the documents.

PART D STATEMENTS BY THE PERSONS SIGNING DOCUMENTS

FOLLOWING THE ABOVE EXPLANATIONS, the borrower stated to me:

- that he/she/they understood the general nature and effect of the documents. It appeared to me that they did have such understanding;
- that he/she/they were signing these documents freely, voluntarily and without pressure from any other person.

PART E IDENTIFICATION OF PERSONS SIGNING DOCUMENTS

The following evidence of identification was produced to me by the borrower:

(1)

(2)

(3)

(4)

(5)

(6)

PART F TRANSLATION/INTERPRETATION

An independent interpreter, _____ was present at this interview with the borrower and interpreted the statements made by all parties. A certificate by the interpreter is held by me.

AUSTRALIAN LEGAL PRACTITIONER'S CERTIFICATE

I CERTIFY the above information.

SIGNED: DATED:

CLIENT'S CERTIFICATE

I CERTIFY that


I have been handed a copy of this certificate.
I have read this certificate.
I am the client named.
The above information is true.

SIGNED DATED:

Law Institute of Victoria / Corporate Print Item 3.1

Australian Legal Practitioner's Certificate 2

(Schedule 2)
February 2006



**FOR USE IN CERTIFICATION WHERE THE PERSON(S) SIGNING IS A
THIRD PARTY, GUARANTOR, SURETY MORTGAGOR OR INDEMNIFIER FOR THE
PRINCIPAL BORROWER**

AUSTRALIAN LEGAL PRACTITIONER'S CERTIFICATE 2

PART A TO:
THIS CERTIFICATE IS PROVIDED BY:

An Australian legal practitioner holding a current practising certificate under the Legal Profession Act 2004 and not acting for you or the borrower in this transaction

I HAVE BEEN ASKED TO INTERVIEW:

(called "the guarantor")

I HAVE BEEN PROVIDED WITH THE FOLLOWING DOCUMENTS:

(1)

(2)

(3)

(4)

(5)

(6)

PART B EXPLANATIONS GIVEN BY THE CERTIFYING AUSTRALIAN LEGAL PRACTITIONER

I CERTIFY that in the absence of the borrower and before the guarantor signed the documents, I EXPLAINED to the guarantor:

- the general nature and effects of the documents required to be signed by the guarantor;
- that if the borrower defaults in payment or in other obligations to you the guarantor would be liable to make good that default which could involve all amounts owed by the borrower to you and substantial arrears of interest.
- that the giving of a guarantee involves considerable risk, including the risk of losing any security, property and other assets and requires very careful thought.

PART C EXCLUDED EXPLANATIONS

I INFORMED the guarantor in very clear terms that I was not expressing any opinion nor advising on:

- the viability of the transaction which the borrower was undertaking, and
- the borrower's ability to make the required payments to you; and
- the client's (guarantor's) ability to make payment to you.

I FURTHER INFORMED the guarantor that if in any doubt on these aspects the guarantor should obtain independent financial advice before signing the documents.

PART D STATEMENTS BY THE PERSONS SIGNING DOCUMENTS

FOLLOWING THE ABOVE EXPLANATIONS, the guarantor stated to me:

- that he / she / they understood the general nature and effect of the documents and the obligations and risks involved in signing those documents. It appeared to me that they did have such understanding;
- that he / she / they were signing these documents freely, voluntarily and without pressure from the borrower or any other person.

PART E IDENTIFICATION OF PERSONS SIGNING DOCUMENTS

The following evidence of identification was produced to me by the guarantor:

(1)

(2)

(3)

(4)

(5)

(6)

PART F TRANSLATION/INTERPRETATION

An independent interpreter, _____ was present at this interview with the guarantor and interpreted the statements made by all persons present. A certificate by the interpreter is held by me.

AUSTRALIAN LEGAL PRACTITIONER'S CERTIFICATE

I CERTIFY the above information. The borrower was not present during my interview with the guarantor.

SIGNED: DATED:

CLIENT'S CERTIFICATE

I CERTIFY that


I have been handed a copy of this certificate.
I have read this certificate.
I am the client named.
The above information is true.

SIGNED DATED:

Law Institute of Victoria / Corporate Print Item 3.2

Certificate by Translator/Interpreter

(Schedule 3)
February 2006



CERTIFICATE BY TRANSLATOR/INTERPRETER

THIS CERTIFICATE IS PROVIDED BY:

NAME:

ADDRESS:

OCCUPATION:

(1) On the day of 20

I attended a meeting at the office of
Present at the meeting were
and

(2) I spoke to
in the
language and I established that is their customary language.

(3) I am fluent in the English language and the
language and I am competent to translate between both those languages.

(4) In the presence of
and
before any documents were signed, I translated the explanations by the Australian legal practitioner and the
statements made by
from the English language to the
language and from the
language to the English language.

(5) It was stated by
that they understood the matters translated and they did appear to me to so understand.

(6) I am independent of and not related to

SIGNED:

DATED:

Law Institute of Victoria / Corporate Print Item 3.3

Form of Acknowledgement Given by Borrower or Surety

(Schedule 4)
February 2006



FORM OF ACKNOWLEDGMENT GIVEN BY A BORROWER OR SURETY TO THE CERTIFYING AUSTRALIAN LEGAL PRACTITIONER

THIS ACKNOWLEDGMENT IS PROVIDED BY ME.....
(name)

of
(address)

.....
(occupation)

to (certifying Australian legal practitioner).....
(called "the Australian legal practitioner")

OF.....
(firm name and address)

I ACKNOWLEDGE THAT:

- the Australian legal practitioner has signed a certificate at my request;
- my name and address is correctly recorded above and on the certificate given by the Australian legal practitioner and I have provided proof of my identity in the manner recorded in the certificate;
- I did attend the office of the certifying Australian legal practitioner on the date recorded in the certificate for the purposes of receiving legal advice on the nature and effect of the documents referred to in the certificate;
- I have received the explanations referred to and have stated to the Australian legal practitioner that I understand those explanations;
- the matters recorded in the certificate are true and correct;
- I confirm these matters by my signature to this acknowledgement and to the Certificate;
- A Translator was present and translated all written and spoken words to me and my responses; or
- A Translator was not required by me as I have an adequate command of the English language.

DATED: the..... day of20

SIGNED:.....

Law Institute of Victoria / Corporate Print Item 3.4

Appendix Two

Practice Note on Solicitor's Certification Procedures

The purpose of this Practice Note

This Practice Note is published by the Law Institute of Victoria. Its purpose is to state the procedures recommended to be followed by a solicitor when engaged to certify an explanation given to a person of the general nature and effect of a loan or security document (including a guarantee) proposed to be signed by that person.

This Practice Note does not apply to a certificate or opinion given by a solicitor for any other reason in connection with a loan or security document.

Application of the recommended procedures

This Practice Note is to be followed when the person signing is an individual and is:

- the direct borrower from a lender or a security provider referred to as a borrower in the document to be signed; or
- a third party guarantor, surety mortgagor or indemnifier for the principal borrower.

This Practice Note applies regardless of whether the relevant transaction is for personal or commercial purposes.

A certificate not in accordance with this Practice Note may not be accepted by the lender.

Independence of the certifying solicitor

The certifying solicitor must be independent of the lender in all instances of certification. Where certification is being given for a third party guarantor, surety mortgagor or indemnifier, the certifying solicitor must be independent of both the lender and of the principal borrower in the subject transaction.

Contents of the certificate

The certificate provided by a solicitor for a borrower or for a security provider referred to in the lender's documents as a borrower shall be in the form of Schedule 1.

The certificate provided by a solicitor for a third party guarantor, surety mortgagor or indemnifier on behalf of a principal borrower shall be in the form of Schedule 2.

Each part of the certificate in Schedules 1 and 2 (as the case may be) shall be fully completed by the solicitor to the extent relevant to the transaction and before the interview is concluded. In particular, the solicitor shall -

- record the name and address of the client;
- record the details of each document with which the solicitor is provided (title and date of document);
- give the explanation referred to in Part B of the certificate;
- give the information referred to in Part C of the certificate;
- be satisfied that the client freely makes the statement referred to in Part D of the certificate and appears to have the understanding referred to. If it appears to the solicitor the client does not have that understanding the certificate must not be signed by the solicitor;
- include in Part E details of the evidence of identification produced by the client;
- where an interpreter is present at an interview with the client, include the name of the interpreter in the certificate and ensure the interpreter completes a certificate in the form of Schedule 3 before the interview is concluded;
- hand the client a copy of the completed certificate, ensure the client reads it and have the client sign the certificate.

Acknowledgment by the client

The Law Institute further recommends that a certifying solicitor should ensure an acknowledgment is signed by the client for retention on the solicitor's file. While the client will sign the foot of the certificate it is recommended that the solicitor's file retain an acknowledgment of those matters and any other relevant matters discussed with the client as are detailed in the form in Schedule 4.

Appendix Three

Rule 8.6 Victorian Lawyers RPA Ltd Professional Conduct and Practice Rules 2005

A practitioner must not act for a guarantor in connection with the loan of money or the provision of finance or an agreement to lend money or provide finance where the practitioner is also acting in the same transaction for the borrower or the financier. Rule 8.6 does not prohibit the practitioner acting for both a borrower and a guarantor if in the same transaction the guarantor is:

- (a) a borrower;
- (b) a director of a borrower;
- (c) a shareholder of a borrower;
- (d) a beneficiary in a trust of which the borrower is the trustee;
- (e) a party holding a beneficial interest in a borrower;
- (f) a body corporate related to a borrower within the meaning of the *Corporations Act*;
- (g) a director of such a related body corporate;
- (h) a shareholder of such a related body corporate; or
- (i) a party holding a beneficial interest in such a related body corporate,

nor does rule 8.6 prohibit the practitioner acting for both a financier and a guarantor in the same transaction if they are related bodies corporate within the meaning of the *Corporations Act*.

For the purposes of rule 8.6, 'guarantor' includes indemnifier, surety or a person or company providing security for a loan or finance.

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