



FINANCIAL SERVICES FEDERATION

16 May 2013

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Dear Cindy

EXPOSURE DRAFT OF LAND TRANSFER BILL

Thank you for your email of 19 April, inviting our comments on the exposure draft of a new Land Transfer Bill (the "draft Bill").

We have reviewed the draft Bill and discussed it with our legal advisers following feedback from members, most notably from those who are mortgage lenders. Those members have had relatively little time to consider the draft Bill or to discuss it with their legal advisers, and it may be that by the time the Bill is ultimately introduced, the comments of the FSF or of members individually may cover a larger range than this letter does.

However in the meantime there is only one specific area of the Draft Bill on which the FSF wishes to comment in this letter, namely clauses 50 and 51 about the proposed obligation the draft Bill will place on mortgagees to verify the identity of their mortgage customers (the "proposed ID obligations").

The Law Commission's proposal that the Land Transfer Act should place such an obligation on mortgagees was of course the subject of discussions between the FSF and LINZ in late 2010, after my predecessor as Executive Director, Kirk Hope, had recorded the FSF's opposition to that proposal in his letter of 27 September 2010.

The FSF's position remains as it was at that time: the FSF opposes the proposed changes to the Land Transfer Act that would place an obligation on mortgagees to verify the identity of their mortgagors, and empower the courts to set aside mortgages where that obligation had not been performed.

As the FSF's reasons for being of that view were set out fully in the FSF's above letter of 27 September 2010, I do not propose to repeat them fully in this letter. However it may be useful if I summarise the key aspects of the FSF's views as follows, before making some specific submissions in respect of these provisions:

- a. The FSF is concerned that the proposed ID obligations erode a fundamental concept of New Zealand's land transfer system, namely that unless a person is themselves fraudulent, a registered instrument gives them indefeasible rights. Such rights in turn underpin the prudential position of mortgage lenders who are subject to either the bank or non-bank deposit taker prudential regimes;
- b. That erosion of fundamental land transfer concepts does not seem necessary: mortgage fraud is not common in New Zealand, and in those few recent cases where litigation has resulted from mortgage fraud, the courts have achieved results that already protect the position of defrauded land owners;

- c. Even if innocent land owners were to suffer loss due to mortgage fraud, they would be entitled to claim under the compensation provisions that already exist in the Land Transfer Act. The proposed ID obligations in the draft Bill would transfer that risk from the public sector to the private sector, in a further erosion of another long standing feature of the Land Transfer system;
- d. The proposed ID obligations also seem unnecessary, in the sense that mortgage lenders are already subject to stringent obligations in terms of identity verification, notably the AML laws soon to come into force. The proposed ID obligations are thus unlikely to achieve meaningful changes in lender practices. Instead, they will only further penalise activity that is already heavily regulated;
- e. The proposed ID obligations are also at odds with Land Transfer Act practices and with LINZ standards which oblige conveyancing professionals to verify the identity of the party executing a mortgage, rather than their mortgagee clients doing so.

As noted above, those factors were more fully explained in the FSF's letter of 27 September 2010.

Although the FSF remains opposed to the proposed ID obligations which the draft Bill will place on mortgage lenders, in case these proposals do ultimately become part of a new Land Transfer Act, the FSF would like to make the following further comments, some with a view to improving any law that may result from the proposed ID obligations:

1. **Clause 51 of draft Bill:** The FSF notes that a transferee of a mortgage will acquire a mortgage subject to the risk of avoidance by a court under clause 50, but does not itself have an obligation to verify customer identity. That is certainly an improvement on the Law Commission's proposals about transferees, which seemed to envisage that a transferee might have such an obligation;
2. **Clauses 52 and 53 of draft Bill:** The FSF notes that these provisions would allow a court to set aside a void or voidable instrument (such as a mortgage) if it would be "manifestly unjust" not to do so. There seems potentially to be a large overlap between these provisions and the proposed ID obligations in clause 51: a fraudulently executed mortgage is arguably a "void or voidable" instrument for example. The FSF –
 - a. Thus has similar concerns about these provisions to those it has expressed at a – e above;
 - b. Also has concerns about Clauses 52 and 53 that transcend the context of mortgage fraud. These clauses will facilitate challenges to registered mortgages that are not presently possible: there are potentially many situations in which it could be argued that a mortgage was "void or voidable";
 - c. Considers this too to be an erosion of indefeasibility, which the FSF also does not support. The FSF would like to better understand the objectives of Clauses 52 and 53 with a view to achieving them in other ways if possible;
3. **Clause 50(1) of draft Bill – whose identity is to be verified:** Clause 50(1) of the draft Bill would require a lender "to verify the identity of the mortgagor and the identity and the authority of any person who executes the mortgage". That is too widely expressed, as it might require the identity of a covenantor or guarantor to be verified. That in turn might mean a mortgage was at risk if a guarantor's identity had not been adequately verified, but that would be inappropriate, as it is only the signature of a mortgagor that can make possible registration of a fraudulent mortgage. If it proceeds, that text should accordingly end "...any person who executes the mortgage *on behalf of the mortgagor*".
4. **Clause 50(2) of draft Bill – Registrar's "standards":** If the proposed ID obligations in clause 50 do proceed, then exactly what that may require by way of customer identification is likely in large part to depend on the "standards specified by the Registrar under section 221" which are mentioned in clause 50(2). About such standards –

- a. The FSF notes that clause 221(2) requires that before making any such standards, the Registrar must “consult with any organisation that represents persons who will be affected.” The FSF considers itself to be such an organisation, and would want to be consulted about any such standards in due course;
 - b. Either the standards, or preferably the text of clause 50 itself, should make clear that a mortgagee may verify the identity of its customers by, in effect, delegating that responsibility to a conveyancing professional. That would align directly with existing practices, as noted at item e in the summary above, and would also align with the fact that the AML legislation permits customer identity to be verified by agents (see section 34 of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (“AML Act”));
 - c. More generally, the impact of the proposed ID obligations on mortgage lenders could be further mitigated by the standards made by the Registrar being as similar as possible to – or even the same as – the practices required by the AML Act to verify customer identity.
5. **Clause 50 (4) of draft Bill –retention of records**: This envisages that a mortgage lender must retain its identity verification records for 10 years. That period differs from other statutory record keeping periods, most notably from the AML legislation where the obligation is to keep identity verification records for 5 years from completion of a transaction. The FSF suggests –
- a. Either Clause 50 (4) of the draft Bill should be deleted as an unnecessary duplication of other statutory obligations; or
 - b. The period for which the records must be kept should be aligned with those in the corresponding parts of the AML legislation (see section 50(3) of the AML Act in particular);
6. **Clause 50 (7) of draft Bill – Setting aside mortgage**: Clause 50 (7) of draft Bill empowers a court to set aside a mortgage where the “mortgagee fails to comply with this section”. That is too generally expressed – a failure to comply with the record keeping obligation should not have that consequence for example, but only a failure to adequately identify the borrower. To achieve that, the text should refer to mortgagee who “fails to comply with subsection (1) of this section”.

The FSF trusts that the above the above is clear and, despite its opposition to the proposed ID obligations in clause 50 of the draft Bill, that the above suggestions may be of assistance. If desired, we would be happy to meet to discuss the above – or any other aspect of the draft Bill where you feel we may be able to assist.

Yours sincerely



Lyn McMorran
EXECUTIVE DIRECTOR

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