



FINANCIAL SERVICES FEDERATION

The Financial Services Federation (“FSF”) is grateful for the opportunity to submit on the Land Transfer Bill (the “Bill”).

Background – the FSF:

By way of background the FSF is the industry body representing responsible and ethical finance and leasing providers in New Zealand. The FSF has over fifty members and affiliates providing first-class financing, leasing, and credit-related insurance products and services to over 1 million New Zealand consumers and businesses. The FSF’s affiliate members include internationally recognised legal and consulting partners. A list of the current membership is attached to this submission as Appendix “A”.

As can be seen from this list, five FSF members are Non-Bank Deposit Takers (“NBDTs”) and are licensed as such by the Reserve Bank of New Zealand, while others are motor vehicle, consumer or plant and equipment financiers. The businesses of such members typically include making loans on the security of mortgages over real property, although the extent to which members do so varies: for some members, mortgage finance comprises a large part of their business, but for others it is a smaller part.

For all of those members, the high degree of security represented by registered mortgages is of real importance to them, both in terms of asset quality and in other respects, such as for the NBDTs where the high degree of security given by registered mortgages is recognised by the favourable risk weighting given them by Reserve Bank of New Zealand.

For all these members, it is important both that the Land Transfer system be efficient and also that the high degree of security represented by registered mortgages should not be eroded unnecessarily.

FSF Submissions - General:

The Explanatory Notes to the Bill record that its objectives include to modernise and generally to improve the New Zealand land title system, including to recognise that in recent years it has become almost exclusively an electronic system. As noted above, it is important to the relevant FSF members that the Land Transfer system be efficient and up to date, and accordingly in principle the FSF supports the objectives of the Bill.

The FSF does however have real reservations about the parts of the Bill that would introduce a requirement for lenders to take steps to identify the identity of mortgage borrowers, in order to address what the Bill perceives as being “the problem of mortgage fraud.” In respect of those provisions, the FSF’s submissions are in summary –

- a) There is no clear need for legislation to address mortgage fraud in this way, and it is questionable if doing so will be effective in any case;
- b) If those provisions nevertheless proceed, it is essential that the Bill make clear that mortgage lenders can rely on conveyancing professionals to perform these obligations on their behalf;
- c) It is also desirable that the Bill avoid unnecessary duplication of similar obligations by aligning the identification requirements of the Bill as closely as possible with the

similar “know your customer” (“KYC”) obligations which lenders already have under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (“AML/CFT Act”);

- d) The record keeping obligations also contained in the Bill should similarly be aligned with the similar obligations in the AML/CFT Act.

Each of those submissions is further explained below, and in addition the FSF will also make a further brief submission on clause 56 of the Bill.

FSF Submissions - Specific:

The FSF makes the following further comments by way of explanation of the submissions summarised at a) - d) above.

There is no clear need for legislation to address mortgage fraud in this way, and it is questionable if doing so will be effective in any case: The Explanatory Notes to the Bill on page 2 refer to clause 54 as being as being necessary to address “the problem of mortgage fraud”. Based on the earlier Law Commission report that led to this Bill, the FSF believes that what is being referred to as “mortgage fraud” is the situation in which a person fraudulently raises money by pretending to be the owner of a property that is not owned by them.

If so, then the FSF questions whether that problem exists to any material degree. None of the FSF mortgage lender members have ever encountered it, for example. The Law Commission report did refer to one case where that type of fraud occurred in 2009, and the FSF is aware of another similar situation in 2008. However it is questionable if 2 such cases in a period of at least 8 year period represents a “problem” which necessitates legislative action of this kind, particularly when the legislative solution proposed by clause 54 will apply to literally thousands of mortgages annually, and in doing so may add to the cost of credit.

It is also worth noting that –

- a) in each of the 2 cases mentioned above¹, the decisions reached by the Courts meant that the innocent landowners did not suffer loss: this suggests that legislative action may not be necessary in respect of any “problem” that may exist here; and
- b) lenders are already subject to significant KYC obligations under the AML/CFT Act. If mortgage fraud continues to be problem despite the existence of those existing KYC obligations, then it seems unlikely that clause 54 will fix any such problem by adding what are effectively more KYC obligations;
- c) clause 54 the Bill will not invalidate all fraudulently executed mortgages in any case, but will only do so where the lender did not take what clause 54(1) refers to as “reasonable steps” to verify the borrower’s identity. It must be quite likely that in cases of sophisticated fraud, the fraud may still occur even if such “reasonable steps” are taken. If so, then in those cases clause 54 will achieve nothing.

For those reasons, the FSF submits that it is doubtful if there is a material problem here which requires legislative action but even if there is, clause 54 seems unlikely to be a good solution to it.

¹ The two cases referred to are the 2009 Supreme Court decision in *Westpac v Clark*, and also *Galuvao v Bridgecorp*, 15/2/10, CIV-2008-404-8217, a decision of Williams J which followed *Westpac v Clark*.

If these provisions proceed, it is essential that the Bill make clear that mortgage lenders can rely on conveyancing professionals to perform these obligations on their behalf: Most mortgages are registered with LINZ under the Land Transfer Act, and the current electronic nature of the register means that mortgage lenders invariably need to instruct a lawyer or other conveyancing professional to register the mortgage on their behalf.

In such cases it is clearly desirable for the lender to be able to rely on the lawyer to verify the customer's identity, including because the lawyer already has such an obligation, as is further addressed below.

However the FSF submits it is not presently clear from the Bill that it would be permissible for a lender to rely on a lawyer to verify the customer's identity in that way. Although the Explanatory Notes the Bill on page 2 of the Bill refer to –

“.. a requirement for the mortgagee *or their agent* to take reasonable steps to verify the identity...”

the reference to an agent does not appear in clause 54 (1), which defines the obligation as being that –

“..the mortgagee must take reasonable steps, or ensure that reasonable steps are taken, to verify ...”

The FSF submits that it is not sufficiently clear from that wording that a lender's obligations can be performed on their behalf by a lawyer or other agent, and suggests that the relevant part of clause 54 (1) should be amended so as to make that clear and so as to read –

“..the mortgagee must take reasonable steps, or ensure that reasonable steps are taken by another person as agent of the mortgagee , to verify ...”

Once that has been made clear, a further point that also needs to be addressed is that as noted above, under present law the lawyer instructed by a lender already has an obligation to verify mortgagor identity, under standards set by the Registrar General of Land.² The FSF assumes the intention is that the identity verification standards for the purposes of clause 54 will be the same, as otherwise there could be two similar standards applying to the same mortgage transaction (even before account is taken by KYC obligations under the AML/CFT Act, which are addressed below.).

Even if that is the intention, it is a sufficiently important point to be made clearly in the Act. The FSF suggests that a new sub clause is added to clause 54 to the effect that where a mortgagee relies on an agent to verify borrower identity, compliance by that agent with any standards applicable to them is also compliance with the lender's obligation to take “reasonable steps” to verify identity for the purposes of clause 54(1).

While that may be what clause 54(2) already intends when it refers to “A person verifying the identity of a mortgagor...”, as above it is not clear at present if that includes a lender's lawyer, and the FSF suggests that should be made clearer in the way it has suggested.

² The standards are set out in LINZ20002, which can be accessed at www.linz.govt.nz/regulatory/20002

The Bill should also avoid duplication of similar obligations by aligning its identification requirements as closely as possible with KYC obligations under the AML/CFT Act: In those cases where a mortgage lender chooses to meet its obligations under clause 54 itself “in house” rather than by relying on a lawyer to do so, it is clearly desirable that the identity verification standards “set by the Registrar under section 234 ” as referred to in clause 54(2) should be as close as possible to the obligations mortgage lenders already have to verify customer identity under the AML/CFT Act, because:

- a) KYC obligations under the AML/CFT Act already require identification to a high level, and what is deemed sufficient to combat money laundering ought also to be sufficient for the purpose of avoiding mortgage fraud;
- b) Lenders have incurred material levels of cost in complying with the AML/CFT Act, and even higher levels of cost will be involved if the Registrar General of Land sets standards under section 234 that are different from those applicable under the AML/CFT Act.

The FSF accepts that this point could be addressed in the standards made by the Registrar General of Land under section 234, when those standards are made. However the FSF considers this point is sufficiently important to place it beyond doubt by addressing it in the Act itself. The FSF suggests that might best be done by including a new subsection in clause 54 that explicitly states that compliance with KYC obligations under the AML/CFT Act also constitutes “reasonable steps” to verify identity for the purposes of clause 54(1).

The record keeping obligations also contained in the Bill should similarly be aligned with the similar obligations in the AML/CFT Act: The FSF notes that clause 54(4)(b) of the Bill would require records of the steps taken and documents used to verify a borrower’s identity to be retained for a “prescribed period”, to be fixed by regulations. In respect of that the FSF and further submits as follows:

- a) Clause 54 places the obligation to keep these records on “The person who verifies the identity of a mortgagor...”. As already noted it is not presently clear enough whether that person can be the lender’s lawyer rather than the lender itself, but if so then it should also be made more clear that the records can be kept by the lawyer on behalf of the lender;
- b) The FSF has submitted above that the Bill’s identification requirements must be as closely aligned to a lender’s KYC obligations under the AML/CFT Act, and it is very likely that the documents used by mortgage lenders to verify identity under the Bill will be the same as, or at least overlap with, those used by it to comply with the AML/CFT Act;
- c) Section 50 of the AML/CFT Act requires those records to be retained for 5 years. It is accordingly very desirable for the Bill’s “prescribed period” also to be 5 years;
- d) That point is sufficiently important that the 5 year period should be referred to explicitly in the Act itself (as it is in the AML/CFT Act) rather than being left to regulations.

Submission on clauses 56 and 57 of the Bill: Clauses 56 and 57 of the Bill provide for a Court to be able to set aside registered instruments where the registered instrument was, prior to registration, “void or voidable” and the court considers it would be “manifestly unjust” not to do so.

There is no equivalent of these provisions in the Land Transfer Act at present, and the FSF has concerns about the scope of clauses 56 and 57, which will make it possible for registered mortgages to be set aside and their registration cancelled, if they are “void or voidable”.

The FSF submits that the term “void or voidable” is undesirably lacking in clarity. One possible example of a “void or voidable” instrument might be a fraudulently executed mortgage, but clauses 56 and 57 are not necessary to deal with that situation, because clause 54 will already do so.

It is not clear to the FSF what other situations might result in a mortgage becoming “void or voidable”, but presumably that might result from non-compliance with another statute. If so, then the FSF is concerned that these new provisions may encourage challenges to registered mortgages due to a range of statutory compliance issues, some of which may be quite technical in nature.

The FSF accordingly submits either that clauses 56 and 57 should not proceed, or alternatively that they should specify exactly which specific types of statutory non-compliance they are intended to relate to.

Once again, the FSF is grateful for the opportunity to submit on the Bill and would be happy to provide any further information that may prove useful.



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A National Federation of Financial Institutions

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Membership List as at 1 March 2016

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