Updating the Land Registration Act 2002

Response by the Council of Mortgage Lenders
to the Law Commission Consultation Paper

Introduction

1. The CML is the representative body for the residential mortgage lending industry that includes banks, building societies and specialist lenders. Our 137 members currently hold around 95% of the assets of the UK mortgage market. In addition to home ownership, CML members also lend to support the social housing and private rental markets. Our members rely on the Land Registry in England and Wales in the course of their everyday business, and have been consulted on this response.

2. We welcome the opportunity to respond to this consultation. Enquiries on the content of this consultation should be sent to jennifer.bourne@cml.org.uk

General Comments

3. Given the breadth of the consultation, we have commented only on the aspects and proposals of most relevance to the residential mortgage lending market. We have answered the specific consultation questions of interest to our members, in the body of this response.

4. The government’s decision about future changes as to who operates the Land Registry may have an impact on some of the issues that this consultation raises, so we welcome the statement from the Law Commission that it will fully take into account any government decision in this aspect, in its final recommendations on changes to the Land Registration Act 2002 (‘the LRA’). We urge them to do so, especially in the case of the indemnity proposals. Lenders rely on the system of land registration, backed by an indemnity, to support mortgage lending and associated funding, and it is important that necessary existing safeguards are in place to maintain confidence in the current structure.

Chapter 5: Powers of registered proprietor and restrictions on the register

5. We agree in principle with the proposal at paragraph 5.30 of the consultation that the LRA is amended to enable a person who has a transfer or grant of a registrable estate or charge in his or her favour to be registered as the proprietor of that estate or charge. We do not however, have any evidence that the current wording of the LRA is causing problems in practice. We agree that formal requirements for registration in relation to s24 LRA would render the current mortgage process difficult, if not unworkable.

Chapter 9: Protection of third party rights on the register Part I: notices

6. In response to the questions set out in paragraphs 9.116-9.121 of the consultation, lenders will use unilateral notices on occasion to protect their interest. For example, if a conveyancer fails to register their charge, a unilateral notice is the only way of recording the lender’s interest in the property. Our members do not consider that there are any major issues with the current process and therefore do not see cause for changing the current procedures. However, if it is seen as appropriate to recommend change, we prefer option 2A as set out in the consultation in relation to adapting the procedure for unilateral notices.

7. In response to the questions at paragraph 9.153 and 9.154, an issue can arise where a loan book is sold and a number of the loans in the book are only protected by agreed notices, due to the fact that the lender was unable to get the charge registered due to the restriction of a prior lender, the Land Registry will not amend the beneficiary of that agreed notice to show the transfer of the loan book. This makes it extremely difficult for the lender to exercise their power of sale which under a Deed they are entitled to do. We would therefore support a change which allowed identification of the
beneficiary of an agreed notice, which in turn would enable updating of the details should the beneficiary change. We think this would make the position of the new beneficiary more secure.

8. With respect to whether this should be mandatory or optional, as long as the ability existed for the Land Registry to update the Register under either framework, we do not have any strong view. There are unlikely to be any particular sensitivity around identifying the beneficiary in the circumstances described in paragraph 7 above.

Chapter 10: Protection of third party rights on the register Part II: restrictions

9. In response to the question posed at paragraph 10.25 of the consultation, we agree with the Law Commission’s view that it should be possible to protect contractual obligations by means of a restriction. First charge lenders will commonly enter restrictions to ensure that they are aware of and consent to any second charges. This is an important protection as it allows the lender to assess whether there is a risk of the chargor being unable to continue to meet their obligations, prior to consenting to any second charge. We agree that there is an onus on the second chargee to search and check the presence of a restriction to minimise any issues. This is especially the case given the relatively common use of such restrictions by first charge lenders.

10. In response to the question at paragraph 10.29 of the consultation, we do not think there is a strong argument to carve out any particular types of contractual obligation from being capable of protection by way of a restriction.

Chapter 13: The guarantee of title – alteration, rectification and mistake

11. We support the aim of more clarity around the circumstances under which the register may be rectified, as well as the other broad objectives when looking the indefeasibility of title. With regard to the proposals to help achieve these objectives:

- We broadly agree with the proposal that where the registered proprietor’s name is removed from the register by mistake (including fraudulent impersonation) that the law should be weighted in favour of returning the land to them.
- We support the retention of the current principle that the law should be weighted towards protecting the registered proprietor in possession.
- We do not have any strong views as to the introduction and length of a long stop period, after which rectification should generally cease to be available, as long as there is still recourse to the indemnity.
- We do not agree that chargees such as mortgagees should not be able to oppose rectification of the register if their charge is registered by mistake. However if the mortgagee can recover any loss by virtue of an indemnity, then it would not wish to oppose rectification.

12. While recognising that a mortgagee’s interest is in one sense, financial only, a charge, once registered, does confer certain rights such as the ability to exercise a power of sale. We are concerned with the principle of carving out exceptions to rectifying the register, based on the characteristics of the potential claimants. As the consultation notes, other proposals made in Chapter 14 may result in a circumstance where the mortgagee could neither claim indemnity nor oppose rectification and we do not support such an outcome. The final proposals should safeguard against this circumstance.

Chapter 14: The indemnity

13. The UK residential mortgage market, represented by CML members, places a heavy reliance on the system of land registration, backed by a state guarantee of title through the provision of an indemnity. This reliance underpins mortgage lending and associated funding, maintains confidence in the secured lending arena and so impacts on the conveyancing process as a whole. We are concerned that some of the changes proposed to the indemnity may erode that confidence.

14. We are also of the view that it is not fair, in principle, to introduce distinctions based on those who can claim and those who cannot, based on a perception as to the extent to which a specific Land Registry user can protect their position. We do not believe it is appropriate to single out stakeholders such as mortgage lenders in this way. This is especially so in cases involving fraud, as the fraud may
not be detectable by any party, even acting as conscientiously as possible, until it has already taken place.

15. At the current time, there is a significant backlog of applications awaiting registration. First registrations and leaseholds in particular are taking months to complete, because of a lack of skilled staff within Land Registry to deal with these applications in a more timely manner. We are aware that the Land Registry has been actively attempting to bring on more resource for some time. However, as the Law Commission notes at paragraph 5.73 of the consultation, this gap between application and actual registration presents risks for those parties relying on the register, which they may need to mitigate.

16. We highlight this issue as it contrasts with the Law Commission’s focus on those other than the Land Registry who have the power to prevent fraud. A swifter registration process would help to lessen fraud risk and this can be achieved by sufficient resourcing of the Land Registry.

Options for revising the indemnity

Option 1: Placing a cap on the indemnity

17. We do not support a cap on the level of indemnity. This is because, in our members’ experience, conveyancing transactions which go wrong can easily see losses in the millions of pounds – recent fraudulent cases uncovered during and after the credit crunch bear this out, and members already experience difficulty when seeking to rely on professional indemnity insurance as a conveyancing client and hitting liability caps within that context. As the consultation paper notes, any cap would need to be at a sufficiently high level to ensure that most claims were met, and therefore may not provide any additional benefits in terms of liability reduction.

Option 2: duties of care and Land Registry

18. While we support the general principle of incentivising best practice to prevent and detect registration fraud, we note the options set out to improve a duty of care for conveyancers or even impose a statutory duty of care will overlay existing professional and legal requirements. Any new duties will need to work in complement with these existing requirements.

Option 3: other options for reform in respect of identity fraud

19. As we note at paragraph 14, identity fraud can be difficult to detect regardless of the checks made by various stakeholders and we have commented on this further below in respect of lenders. We recognise that the Land Registry is not necessarily best placed to establish if there are potential fraud indicators, depending on the type of fraud being perpetrated. Broadly, we support a collaborative approach between stakeholders to help prevent and detect identity fraud in the context of property transactions and we engage with the legal sector and the Land Registry on a regular basis to discuss ways of tackling property fraud.

20. With regard to rationalising ID requirements, we have been discussing with the legal sector in England and Wales, some potential changes to the CML Handbook to provide one set of instructions within the section that deals with identity and signatory requirements, rather than differentiate between segments of the conveyancing market. Again, it is important to reflect the differing regulatory and legislative obligations to which professionals are already subjected.

21. We support in principle, the enhancing of Land Registry powers in relation to identity checking. We have previously discussed the use of Verify with Land Registry; and our members can see some benefits in the use of such a model. It is important that Land Registry consult with their stakeholders on potential models following their own research to ensure that there is appropriate buy-in and that the model can work with the existing requirements for property professionals and those who provide finance for property.

Option 4: limiting the circumstances in which mortgagees can claim indemnity
22. As we stated earlier in this response, our members rely on the system of land registration, backed by an indemnity, to support mortgage lending and associated funding, and it is important that necessary existing safeguards are in place to maintain confidence in the current structure.

23. While lenders do not make decisions to lend solely on the basis of the existence of the indemnity (also taking into account a range of regulatory and risk-based requirements in deciding whether to lend) the fundamental structure of the land registration system in England and Wales, including the support of the indemnity, provides the necessary confidence for lenders to be able to lend in the knowledge that they will have a legally enforceable security; and protection in the case of error or fraud.

Option 4A: limit ability of mortgagees to obtain an indemnity to transactions entered into on the basis of mistakes in the register

24. As mentioned at paragraph 14 above, we do not think it is justifiable to limit the circumstances under which a stakeholder such as a mortgage lender can claim an indemnity. We can see no reasons why lenders should not be treated the same as other stakeholders in the conveyancing/mortgage process. This is especially so in fraud cases, when, even acting as conscientiously as possible, a mortgagee may not detect a fraud until it has already taken place.

Option 4B: a statutory duty to verify the identity of mortgagors

25. We note the comment that the rationale for imposing specific duties on mortgagees is that lenders are seen as best placed to prevent identity fraud. We question whether this is the case, and why lenders are singled out, given the way that the house-buying and mortgage markets operate in England and Wales.

26. It is certainly correct that lenders carry out checks on their prospective borrowers and they carry out these checks without exception – we comment further on the obligations on lenders in this regard in paragraph 27 below. However, conveyancers in a property transaction will equally be required to carry out such checks and so are at least as well-placed as lenders to prevent identity fraud. It could be argued that conveyancers are in fact best placed as they effectively control the purchase transaction and in doing so have direct contact with all the other stakeholders in the transaction - a unique position. Having said that, the sophisticated techniques fraudsters use may go undetected by the most conscientious of conveyancers and lenders, which is why we support a collaborative approach to fighting fraud.

27. It is important to emphasis that mortgage lenders are under regulatory obligations to prevent fraud, including verifying their customer’s identity and carrying out due diligence on their customers and their professional service providers, such as lawyers and valuers. For example:

- The FCA Handbook SYSC 3.2.6R and SYSC 6.1.1R requires firms to establish and maintain effective systems and controls to prevent the risk that they might be used to further financial crime – this includes verification of potential customers;
- Firms must comply with Principles 1 (integrity), 2 (skill, care and diligence), 3 (management and control) and 11 (relations with regulators) of the FCA Principles for Businesses, which are set out in PRIN 2.1.1R;
- The Statements of Principle for Approved Persons set out in APER 2.1.2P; and
- In relation to guidance on money laundering, the rules in SYSC 3.2.6AR to SYSC 3.2.6JG and SYSC 6.3 (Financial crime).

The FCA guidance for firms on preventing financial crime summarises mortgage lenders’ obligations.

28. We do not accept, therefore, the implication made in the consultation at paragraph 14.120 that mortgage lenders are not incentivised to develop best practice around fraud prevention as they will not bear the cost of fraud which affects their security. On the contrary, if a lender was found to be in breach of their regulatory requirements in relation to fraud prevention and controls, they could face substantial penalties imposed by their regulator. In addition, depending on the type of fraud, a lender may need to claim as a client under other indemnity cover, or pursue their losses through the courts, which often carries the risk that the losses are not fully recoverable. Lenders have reported significant losses in relation to mortgage fraud in recent times. Replacing the indemnity by instead
relying on title insurance is not desirable, as this is an untested market from a lender’s perspective and it would inevitably create uncertainty as to the level and degree of cover which would be obtainable.

29. In terms of other effects of proposals to limit the circumstances under which mortgagees can claim an indemnity, lenders would need to consider how the removal of an indemnity impacted on their ability to securitise loan portfolios. Our preliminary view is that limiting the ability of mortgage lenders to claim under the indemnity may impact on current securitisation agreements. The existence of any indemnities such as that provided by virtue of the LRA are currently taken into account; and the lack of such an indemnity going forward would need to be factored into future agreements. There may be an impact on mortgage portfolio trading in terms of lower prices paid for assets, in light of the increased risk.

30. Finally, as the consultation notes, the separate consultation on the privatisation of the land registry contemplates that the indemnity would remain in its current form. It does, however, contemplate that the operator may have a financial stake in the level of indemnity. In our response to that consultation, we raised concerns as to how this would incentivise the operator to reject claims made under the indemnity to minimise their financial stake. This consultation introduces a new concern that the reassurances made about the existing indemnity staying in its current form may not hold. This creates additional uncertainty about the impact of a change in the operation of the Land Registry and is not well-timed in the context of the wider discussions about privatisation.

Chapter 18: Further Advances and the law of mortgages

31. We are not aware of any particular issues being caused as a result of s49 of the LRA in relation to tacking, from a residential mortgage perspective. Some of our members have noted that they would prefer the certainty of using Deeds of Postponement for the crucial aspect of ensuring priority of the first-charge mortgage.

Chapter 20: E-conveyancing

32. We agree in principle that the LRA should be amended to introduce better flexibility for the introduction of e-conveyancing. We are pleased that some of the legal issues which presented difficulties for practitioners and lenders alike are being considered. We agree with the proposals for the LRA to be amended to clarify:

- The position of trustees who rely on a single practitioner to sign electronic transfers on their behalf
- How the beneficiaries’ interest can be overreached where the trustees grant a single conveyancer the power to sign e-conveyances and give receipt for capital monies

33. We note that the forthcoming BIS review of the home buying and selling process may choose to focus on improving the land registration system; and that e-conveyancing may ultimately be a focus for reform.

Summary

34. While we welcome some of the proposals aimed at improving clarity, and removing some operational difficulties caused by the LRA 2002, we are concerned that there is not sufficient justification for the proposals relating to limiting the mortgagee’s ability to claim an indemnity and we would urge caution in taking forward radical changes to the indemnity scheme, as this may have wider unintended impacts. We are also conscious that reform of the indemnity is being proposed at a time when not only is the future of the Land Registry uncertain, but, with the EU referendum result, wider economic uncertainty now exists, with it’s potential impact on the housing and mortgage markets. The proposals in this consultation in relation to indemnity introduce further uncertainty, and we hope that the Law Commission recognises this in considering its final recommendations.

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