

News flash

Mortgage Fraud: Do not be an unwitting participant

Judy Gibson reviews the latest Law Society guidance on mortgage fraud.

Last month, the Association of Chief Police Officers announced it was clamping down on mortgage fraud following the revelation that the industry had been swindled out of £700 million through various scams. This followed the FSA's announcement that it was working with police forces to investigate and fight mortgage fraud. In fact, the City of London fraud squad had already joined forces last year with the Serious Organised Crime Agency, as well as the Serious Fraud Office to launch a detailed investigation into commercial property fraud in the West Midlands.

The Law Society published a practice note on 18 March 2008, to enable solicitors to protect themselves from being unwittingly caught up in mortgage fraud. The Courts and SRA will expect compliance with this statement of good practice. A summary of the main points and some practical guidance follows:

Individual or small-scale frauds

When the loan application does not accord with the solicitor's knowledge or information regarding the purchase, this could indicate mortgage fraud. Examples are:

- Personal information: the borrower's identity, income, employment, other debt obligations
- Sources of funds other than the mortgage for the purchase
- The value of the property
- Direct payments between purchaser and seller.

Solution: Check the detail on the loan documentation and background to the transaction. If there are discrepancies

challenge your borrower client and if they will not cooperate refuse to act.

Large-scale frauds

Common indicators tend to be use of non-bank lenders, inflated property value, fictitious nominated purchasers and a chain of back-to-back transactions with an increasing price/valuation at each stage. Particular diligence is needed in packaged and/or buy-to-let transactions.

Look out for the following warning signs and ask questions:

Identity:

- A single client or property transaction that is not local to your firm. Why not use a local firm (unless a bulk instruction)?
- A corporate purchaser: Is it an arms length transaction?
- First time property investment of this scale. Why this venture and where is the financial backing coming from?
- The current owner has owned the property for less than 6 months. Why are they selling?

Value:

- A significant or disproportionate increase in value over a short period of time.
- 100% mortgage.
- Incentives, allowances or discounts including cash back, fittings and white goods, payment of legal fees. Have these all been properly disclosed to the lender?
- Deposit is being paid by someone other than the purchaser.



- ▶ • Direct payment of deposit from purchaser to seller.

Obtaining consent to pass information to the lender

The solicitor owes a duty to his lender client to disclose any information material to the lending decision. This duty is overridden by the duty of confidentiality to the borrower client (Code of Conduct Rule 4.01) except where satisfied that there is a strong prima facie case of fraud or other criminal purpose.

Solution: Include a section in your standard terms and conditions which provides that you will advise the lender client of any relevant information arising during the retainer.

Hints to avoid consent being disputed:

- Bring this term to your borrower client's attention at the outset of the retainer
- Do not act until you have the borrower client's signature accepting your terms and conditions

If your client refuses consent for disclosure of relevant information to the lender, cease acting.

Solicitors can be liable for mortgage fraud even if they are not aware that the fraud has taken place

Liability does not require active participation, or even knowledge of the fraud. The definition of fraud has been extended by the Fraud Act 2006 to include false representation (implicit or explicit) and failure to disclose information where there is a legal duty to do so.

Solution: Due diligence. Courts will be more sympathetic to a solicitor who has exercised due diligence and complied with the Law Society guidance note.

Hints:

- Identify your client and all parties associated with every transaction, including the conveyancers and solicitors.
- If an existing client asks you to rely on former identity checks (the money laundering 'reliance' exemptions) this may be a risk/indicator in itself. Ensure any previous identity checks you rely on have been fully carried out.
- Scrutinise the documentation for any anomalies, for example in purchase price, direct payments or back to back sales.

- Do not let your client sign any incomplete documentation. This will minimise the scope for fraudulent insertions.
- Raise further enquiries, document the responses and ensure you have passed them on to both lender and borrower clients (subject to confidentiality).
- Do not bow to pressure to not comply with the CML handbook.

Solicitors who are victims of mortgage-fraud attract liability for money-laundering under the Proceeds of Crime Act 2002

If a mortgage is obtained by fraud, it is a proceed of crime. As soon as the loan is forwarded to a solicitor's account to be held pending completion, that solicitor will have acquired, had possession of and/or entered into an arrangement in respect of the transfer of criminal property.

Solution: Report the existence of any proceeds of crime to the practice Reporting Officer. Do not tip off your client if you suspect fraud until you have reported the suspicious practice.

Hints:

- Due diligence should identify the potential fraud before loan monies are received into client account.
- Ensure the solicitors in your team have up to date money-laundering training and are aware of the existence and identity of their Reporting Officer.

Professional Indemnity position

As soon as you are aware that you may have been caught up in mortgage fraud: notify your professional indemnity insurers. Failure to do so or delay in notification could jeopardise your policy coverage. If in doubt, speak to your broker.

If you would like to know more about the practice note, its impact on your practice and your insurance arrangements, please contact:

Judy Gibson

T +44 (0)333 010 5952

F +44 (0)870 839 0960

E judy.gibson@robinsimonllp.com

We can put together a seminar/talk or panel discussion on the issue above, or any of the issues featured in our publications to be held at any of our offices, or yours. If you are interested, please contact any one of our lawyers or David Simon at david.simon@robinsimonllp.com.

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London

Minster House
42 Mincing Lane
London EC3R 7AE
T +44 (0)333 010 0000
F +44 (0)333 010 0001

Leeds

2 St David's Court
David Street
Leeds LS11 5QA
T +44 (0)333 010 0000
F +44 (0)333 010 0003

Manchester

Arthur House
Chorlton Street
Manchester M1 3FH
T +44 (0)333 010 0000
F +44 (0)333 010 0006

Birmingham

37a Waterloo Street
Birmingham B2 5TJ
T +44 (0)333 010 0000
F +44 (0)333 010 0005

info@robinsimonllp.com

www.robinsimonllp.com