

PROPERTY LAW AND EQUITY REFORM COMMITTEE

GUARANTEED SEARCH NOTES

WORKING PAPER

Criticism and comment is invited on this paper.
Submissions to be submitted to the Secretary, Property Law
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INTRODUCTION

1. The attention of the Committee has recently been drawn to the apparent gap in the protection the Land Transfer Act 1952 affords to a purchaser during the period between searching the vendor's title and registration of the purchaser's documents. The Committee has obtained the consent of the Minister of Justice to investigate the position, and, if thought necessary, to suggest a remedy.

THE PROBLEM

2. The existence of the gap has been recognised for a long time - see, for example, In re Jackson's Claim (1892) 10 NZLR 148, where a search (through a failure to check the journal) did not disclose an instrument lodged but not yet entered on the title. But the total gap in protection is much wider than described in that case. It really consists of two distinct parts, in this paper termed "the searching gap" and "the settlement gap". The searching gap refers to the virtual impossibility of discovering whether there are documents lodged but not yet registered at the time of the search, and the risk of further documents being registered after completion of the search but before settlement. The settlement gap is the vulnerability to adverse interests that may be registered after settlement, but before registration.

3. The profession and the Registry have largely turned a blind eye to the danger, partly because it is difficult to remedy, but mainly because the inherent honesty and solvency of the community has meant

that losses caused by hostile liens etc. very seldom occur. However, the recent decision of O'Regan J. at Hamilton in Bradley v. Attorney-General (noted in Current Law, 19th April 1977 at p.69 and in Recent Law May 1977 at p.111), where solicitors sustained a loss of \$5,000, shows that the danger is real and could strike any purchaser or solicitor at any time. Accordingly, the Committee considers that it is desirable to devise some form of further protection for the purchaser in respect of the searching gap and the settlement gap.

THE SEARCHING GAP

4. Except by the making of almost impossible inquiries, a normal careful search does not disclose adverse interests which are in process of registration but are not yet recorded on the title. (The Committee omits discussion of a journal search because under the new procedure it is no longer feasible.) Until the new sextuple abstracts were introduced, it might have taken a week (or even, in some Registries, several weeks) before a memorial could be entered on the title and thus give notice of an adverse interest to a searcher. Fortunately, this gap has been reduced to one or two days - the time taken for a copy abstract to be processed and placed with its copy title in the cabinet, and thus to become automatically available for the information of a searcher.

5. Furthermore, in the case of caveats and liens the Registry has closed the gap even further by the simple but useful expedient of making a pencil note on the title, to alert searchers, within a couple of hours of the lodging of the caveat or lien. But even if the Registry could cut down the time lag on all types of documents to an hour or less, no search is ever final, because obviously adverse documents may arrive at any time after the search is made. This is particularly vital in the case of a check search that a careful conveyancer will make before paying over the purchase price on settlement. There is the abovementioned risk of liens "in the pipeline" but unrecorded while the check search is actually being made, and in addition, even in the time taken to walk from the Registry to the vendor's office for settlement, a further adverse

lien could conceivably be lodged. This double time gap and the consequent risk is obviously very much greater with country settlements because of the physical difficulty of getting up-to-the-minute searches delivered to country towns. The problem is, therefore, to devise a search note on which the purchaser's solicitor can absolutely depend throughout the conveyancing process without danger of adverse interests obtaining registration ahead of the purchaser's documents.

THE SETTLEMENT GAP

6. According to the universal practice in New Zealand, settlements are made in a legal office (either in a registry town or in a country town as the case may be) by paying over the purchase money in exchange for the title and the signed but unstamped transfer and other necessary documents. This is the "point of no return" for the purchaser, and no possible improvements in searching procedure after this point can help him. Documents still have to be stamped, and then prepared for registration by the solicitor (a total process that may take a week or even a month or more, especially with country settlements) but all this time the Registry title is lying in its cabinet vulnerable to liens and other interests that may still be lodged, adverse to the vendor's estate that has not yet been removed from the register. This may mean a devastating loss to the purchaser. Certain incomplete safeguards may be taken by the purchaser (e.g. a caveat) but the Registry should aim to provide a registration system that is proof against this residual amount of risk in the vital process of change of ownership.

NEW DANGERS UNDER MATRIMONIAL PROPERTY ACT 1976

7. The Committee feels strongly that the risk of last minute adverse claims that may endanger or at least delay and embarrass a genuine purchaser has been substantially increased by the right of a spouse to lodge a notice of claim under s.42 of the Matrimonial

Property Act 1976, Such a claim has the effect of a caveat and may be lodged while a sale is in process of settlement, even after the purchaser's last minute check search has been made. A purchaser in good faith who has altered his position in reliance on having an indefeasible interest can get protection under the Act, but the delay, worry, and cost of securing protection might be very great. The safeguards to be suggested in this paper would give protection against such a danger as well as against the older dangers of caveats and liens.

EXISTING SAFEGUARDS IN NEW ZEALAND

8. Various measures of careful conveyancing can be adopted to reduce the risk, but none of them is completely satisfactory.

- (a) Obtain the title on settlement: This is an elementary precaution that eliminates the risk of competing transfers or mortgages being registered against the title after settlement, but does not eliminate the risk of liens or caveats or other documents that do not require production of the duplicate title. In Bradley's case, the purchaser's solicitors did not obtain the title (it was in process of issue in the Registry) and hence a third mortgage of \$5,000 was able to slip in unknown to them and be registered as an adverse interest.
- (b) Prompt registration: This is most important and can proportionately reduce the period of risk, but not eliminate it. With Stamp Office requisitions and unavoidable delays, a lapse of several weeks may be no fault of the solicitor.
- (c) Lodge a caveat: This is a considerable safeguard but does not absolutely settle competing equities and does not prevent lodging of adverse claims or other caveats. It is also too cumbersome to be adopted, except in isolated cases of suspected risk.

(d) Settlement in the Registry: In important cases where adverse interests are suspected, it is possible to arrange for pre-stamping of documents and settlement in the Registry with immediate presentation of the documents for registration, but even then it is necessary to hold back part of the purchase money until the possible existence of adverse documents in the pipeline has been eliminated and until the purchaser's transfer is actually entered and the memorial signed. This is therefore a cumbersome and impracticable precautionary measure, except in very special cases,

9. Precautions (a) and (b) above should be routine procedure, and, if used, will give protection against adverse registered transfers or mortgages but not against caveats or liens. Precautions (c) and (d) are more effective and are practical in individual cases, but are quite impossible as a routine on all transactions. Last year over 130,000 transfers were registered in New Zealand, and if a caveat had been lodged or a registry settlement arranged for every one of these, the registries would have been utterly swamped.

OVERSEAS PROCEDURES

10. In England, and in Western Australia and Victoria, a purchaser may, with the written consent of the proprietor, obtain from the Registrar an official search and a stay order that freezes the title for a limited period and gives priority to the purchaser's document. In the Australian States referred to the period is only 48 hours and, probably for this reason, the procedure is not often used. In England the period is a maximum of 29 days and the procedure is very widely used. But if adopted in New Zealand as the main safeguarding protection, although it would be effective, it would mean major change to our conveyancing and a virtual doubling of the registry workload.

11. It may be that a procedure more suitable for New Zealand conditions is the priority notice system that has been in force in Tasmania since 1973. In that State, the purchaser may lodge such a notice with the Registrar, and the effect is to postpone registration of any other documents for 30 days, so as to grant absolute priority to the purchaser's intended transfer (and the accompanying mortgages) if successfully registered in that period. There are elaborate incidental regulations, which the Committee has studied and taken into account in framing its own proposals, but it is not necessary to outline these here.

THE BASIC CAUSE

12. The basic cause of these gaps is not the fault of the Registry, nor any general lack of skill and care by solicitors, but is due to a peculiarity in the Torrens structure. This is the fact that certificates of title are issued in duplicate, one copy for the owner and one copy for the Registry; and, of these, the Registry one is the master copy. All normal transactions (transfers and mortgages) must be recorded on both copies, but the documents that cause by far the greatest risk (caveats, liens, and spouses' notices of claim) can be registered on the Registry copy only, notwithstanding that other genuine transactions are already under way. This is like the position of a man keeping his money in a bank safe that has two duplicate keys, one kept at home and one at the bank, but with an arrangement that creditors can get easy access to the bank key without the man's consent or knowledge and thereby can defeat cheques already issued in good faith.

GENERAL CONCLUSIONS

13. The remedy that is required for New Zealand conditions should be simple but comprehensive. It would be futile to remedy only the now greatly reduced searching gap but to leave open the very much more serious settlement gap. The remedy should not involve a major change in New Zealand's long established conveyancing practices or

clog up the registries or legal offices with a vast duplication of safety documents. Also it is most important that the remedy must not relieve the legal profession from taking all the right and proper safety precautions that a skilled and careful conveyancer regularly observes in his work: the remedy must merely eliminate the inherent risks that have been described above, and which the careful conveyancer cannot reasonably guard against at present.

14. When weighing up all these considerations, it must be remembered that the risk of loss is statistically very low, in that a loss may occur in only one case in perhaps a million. This points strongly to the conclusion that the remedy should be a form of insurance or indemnity against possible loss, rather than the general introduction of new safety documents. On the other hand, with properties of high value, the possible loss may be very large and these properties will number only a small proportion of the total transactions, it may be justifiable to require a special safety document or procedure to physically prevent the loss in these exceptional cases.

15. Different members of the Committee have devised three different proposals, all of which have certain advantages and drawbacks. Without wishing to evade the responsibility of deciding between the various schemes, the Committee feels it will be better at this stage to submit them all to the profession and interested parties in this working paper, and to invite criticisms and opinions. In due course, after considering the replies, the Committee will make a final recommendation to the Minister.

POSSIBLE REMEDIES

16. Plan A proposes the adoption in New Zealand of a system of Priority Notices similar to that in force in Tasmania and other former British Colonies. The solicitor for a purchaser (or mortgagee or lessee etc.) desiring protection against possible adverse

documents would apply for a Priority Order from the Registrar that would give the purchaser absolute priority of registration for, say, 30 days. Even the members of the Committee who do not support this Plan admit that the method would be effective, but argue that, if adopted for a majority of transactions, it would involve an intolerable addition to the paper work of solicitors and the registry and is therefore unsuitable. However, they do accept that the Priority Notice procedure might be considered with advantage in the very limited number of transactions where the consideration exceeds, say, \$100,000 (an estimated 3% of all transactions). The proponents of Plan A argue that it would not unduly increase the workload of the profession or the Registry, even if adopted generally.

17. Plan B requires the State to take responsibility for the "gaps" in the Registry system and to give an automatic insurance or indemnity to every purchaser for value (including mortgagee, lessee, etc.) who suffers loss from an adverse caveat or lien etc. that was not disclosed by the purchaser's search of the title if made within 14 days before settlement. The period of protection would run from the date of the search through to registration. The Plan would give the State a right of contribution by subrogation against the purchaser's solicitor in any case where the latter was negligent in making the search or in conducting the settlement. The opponents of this Plan object to putting an indefinite burden on the State, particularly by having no limit on the time for completing registration, and also argue that the determination of what would constitute negligence on the part of the purchaser's solicitor is left far too vague. As an improvement they propose the final Plan C.

18. Plan C is more radical and argues that the main risk comes from caveats and liens, which are given unduly favourable priority by the Act at present. The proponents of Plan C propose to give a purchaser's search note automatic priority over liens and caveats not shown in the search, provided that the settlement takes place within

14 days of the search. In other words, liens and caveats are postponed until they have stood on the register for 14 days as a warning of their adverse existence to intending purchasers.

19. The Committee now sets out in more detail the three proposals.

PLAN A

20. As stated above, this proposal involves the introduction into New Zealand of priority notices. It is envisaged that a person seeking protection for any transaction entered into with the registered proprietor could apply to the Registrar for a priority notice. The application would be made in the prescribed form, and would sufficiently identify the estate or interest in the land being dealt with, the nature of the dealing, and the consideration. The consent of the registered proprietor to the issue of a priority notice would be required, and this would be endorsed on the application. The Registrar would have the usual powers to reject applications where errors or omissions occurred.

21. When an application for a priority notice was accepted by the Registrar, it would be deemed to be the priority notice. The Registrar would then enter and sign an appropriate memorial in respect of the notice on the affected certificate of title in the register. From that time on for a period of 30 days, no instrument or dealing (including liens and caveats) affecting the estate or interest protected by the notice could be registered. As against each other, any instruments presented during the period would have priority as if no such notice had been entered. The notice would cease to have effect on the registration of the dealing protected by it.

22. If the period of protection expired and the dealing was still not registered, no further protection by way of priority notice could be obtained.

PLAN B

23. The proponents of this Plan argue that the problem exists because the State (no doubt, for sound policy reasons) has enacted laws, such as the Wages Protection and Contractors' Liens Act 1939 and the Matrimonial Property Act 1976, that allow registration of various interests in or over land without production of the duplicate certificate of title. It has further confounded the problem by being unable to ensure a complete absence of delay between searching and final registration. In other words, despite the highest possible standards of skill, diligence, and expedition on the part of purchasers and their solicitors, losses of the kind referred to above can still occur. Accordingly, it is argued that the ultimate responsibility for ensuring that a purchaser does not suffer loss by using the State-sanctioned (and compulsory) registration system must lie with the State.

24. The searching gap would be closed in this way. Every search note would be "guaranteed" correct as at the time of its issue and for a period thereafter of, say, 14 days. [This guarantee would be effective only against interests that may be registered without production of the duplicate certificate of title.] It would mean that, provided settlement occurred within 14 days of the issue of the search note, the purchaser (or mortgagee or lessee etc.) could rely on a State indemnity against any loss he might suffer from the registration of any adverse interest lodged before the issue of his search note, or between the issue of his search note and the date of settlement. If, for any reason, settlement were deferred beyond the 14 days, a further search note would be obtained and the same protection would then be available for a further 14 days.

25. The registration gap would be closed in an even simpler manner. The State would be required to indemnify a purchaser (or mortgagee or lessee etc.) against any loss suffered by him as a result of the registration of any adverse claim after settlement but before

registration. It is stressed that what is looked for is a State indemnity. The vendor, and, in the case of negligence, the purchaser's solicitor, would remain liable, and the State would be entitled to seek recovery by way of subrogation accordingly.

26. The proponents argue that this scheme has the following advantages:

- (a) It is simple.
- (b) It does not involve any more work for the profession or the Registry Office (except that search copies may need to be "timed" as well as "dated").
- (c) It involves no further documents.
- (d) It does not interfere with the rights of lienholders and others, nor do violence to any fundamental principles of the Torrens system.
- (e) It is cheap. The only extra cost to the State would be the amount of any claims paid out less any amounts recovered through subrogation.

PLAN C

27. This Plan is based on the fundamental cause of the gap in protection as outlined in paragraph 12 above, that is, the fact that the documents that cause the risk (liens and caveats) are registered or noted on the Registry copy of the title only and get immediate effect without any notice or warning to a purchaser in the act of dealing bona fide with the owner's title.

28. After registration of a purchaser's transfer, the Act gives the purchaser an indefeasible title. But it does not give this

protection in the difficult period between searching and settlement and registration, and yet this is the most vulnerable period of all. It is all very well to promise absolute protection after registration, but this is illusory if it is not possible to obtain immediate registration at the moment it is most needed, the "moment of no return" on settlement, and it is worse still when adverse interests (liens and caveats) are given immediate validity the moment they are noted on the registry title.

29. The proponents of this Plan adopt the argument put forward in support of Plan B (paragraph 23) that "the ultimate responsibility for ensuring that a purchaser does not suffer loss by using the State-sanctioned (and compulsory) registration system must lie with the State". But they contend that this can be achieved in different ways. Plan A proposes the adoption of a system of priority notices which would be effective but cumbersome. Plan B does not remove the basic cause, but proposes a remedy in the form of a State indemnity (of an indeterminate amount). Plan C is designed to tackle the cause itself by adjusting what is considered to be the excessive priority presently afforded liens and caveats.

30. The essential elements of Plan C are as follows:

- (a) Every lien or caveat shall take effect against the existing registered proprietors and his estate or interest in the land in accordance with the succeeding subparagraphs of this paragraph.
- (b) As against any bona fide intending purchaser for value (including mortgagee, lessee, etc.) the caveat or lien shall not take effect unless it has been entered by memorial on the Register and has stood there for a purchaser to see for 14 days before the purchaser completes his settlement in pursuance of a search that did not disclose the lien or caveat.

- (c) If a purchaser has made a search that shows no sign of a lien or caveat and if he completes his purchase by settlement within 14 days and obtains the title and a valid transfer, he shall be entitled to registration of his transfer and following mortgages etc. on the title in absolute priority to any later lien or caveat.
- (d) The priority under subparagraph (c) shall be conditional upon the purchaser registering his transfer within one calendar month of the date of settlement.
- (e) If the purchaser sees that, through a hold-up in the Stamp Office or other delay, he cannot register within one month he may secure provisional priority by lodging within one month of settlement a certified copy of the transfer and a certificate detailing the reason for the delay.
- (f) If a caveator or lienor finds that a transfer is presented that claims priority under the above provisions, he may challenge the validity of the transfer or its right to priority by application to the Court (or consider, perhaps, application to the Registrar or the Registrar-General to relieve the burden on the already overworked Court system).
- (g) If the caveator or lienor does not obtain an interim order from the Court or Registry provisionally supporting his caveat or lien within one month (or perhaps two months), then the purchaser shall forthwith be entitled to registration of his transfer and subsidiary mortgages in priority to the caveat or lien.

31. A necessary exception to the above postponement of liens and charges etc. is that certain statutory charges, e.g. for arrears of rates, would not be postponed to a following transfer, because the transferee can and should inquire about arrears of rates before settlement.

32. Certain charges could obtain immediate protection by arranging to be entered on the owner's title as well as on the Registry title. For example, a purchaser under a long-term agreement wants to register a caveat and he can easily, as a term of contract, arrange to have the caveat noted on the owner's title thereby giving positive notice to any later searcher, and so void postponement.

33. A possible compromise to secure the best of both worlds is as follows:

(a) Adopt either Plan B or Plan C (as may be finally determined), but limit it to transactions up to \$100,000, so as to limit the burden on the State, or on lienors and caveators, as the case may be.

(b) For transactions above \$100,000 adopt Plan A. This means that the more cumbersome procedure of Plan A would apply to only about 3% of all transactions and would not impose too much extra work on the profession and the Registry.

POSTSCRIPT - PLAN D

34. After this paper had been prepared a new proposal was received from an outside source which the Committee has decided to include as Plan D.

35. This proposal first of all mentions the possibility of a "priority system" (similar to Plan A) but rejects this because of the necessity of perhaps 100,000 extra registrations a year. Plan D then refers to the distinction between transactions requiring production

of the owner's title such as transfers and mortgages, and those in a second category, such as caveats, liens and charges (not noted on the owner's title) which are the main cause of danger. The Plan suggests the following procedure:

- (a) Just prior to settlement a check search would be made (this would automatically show the date of the search).
- (b) Documents would have to be presented for registration within a certain number of days (very few) of the date shown on the search and the search itself could be lodged with the abstract as evidence that priority is being claimed.
- (c) If registration were blocked by some hostile instrument being lodged and being within the second category the registration would take precedence over the hostile instrument. In these circumstances the District Land Registrar would be required to use his requisitioning powers and not rejection powers if there were any defect in the document presented for registration because rejection would not allow representation within the short time limit contemplated under (b) above and the hostile instrument might prevail after all.
- (d) The party presenting the hostile instrument would be notified of the other registration taking precedence and could immediately pursue the in personam remedies almost always likely to be still available. To the extent that these might fail (and would otherwise have succeeded) as a result of the intended registration the insurance fund would pay out.
- (e) Claims on the fund would be limited to persons who suffered loss through the operation of the legislation envisaged by this proposal and who were not able to

obtain personal redress from the person against whom the right-of-action existed. It seems that the operation of such a system would result in minimal claims and the insurance fund would assume the function for which it is intended.

SUBMISSIONS

36. The Committee invites criticism and comments with a view to further consideration by the Committee of conflicting Plans or any new proposals. The Committee would be grateful if such criticism and comments could be sent to:

The Secretary
Property Law and Equity Reform Committee
Department of Justice
Private Bag
Postal Centre
Wellington

on or before 31 July 1978.