

Editor's note:

ESSAR Insurance Services Limited, Managers of the Professional Indemnity Scheme, in collaboration with Panel Solicitors Howse Williams, issue this quarterly bulletin to highlight risk management issues learned from their handling of claims.

## **Identity Fraud in Property Transactions**

Hong Kong has recently seen a marked increase in crimes involving identity fraud. This is of direct concern for the solicitors' profession, because many of these cases involve property transactions. The Law Society recently published an alert (see Law Society Circular 25-198 (PA)) drawing practitioners' attention to two common *modus operandi* employed by criminal syndicates in recent property fraud cases, as identified by the Commercial Crime Bureau.

This bulletin will look at some specific instances of transactions which have led to claims against solicitors, the applicable legal principles, and the steps that can be taken by solicitors to reduce the risk of claims arising from identity fraud.

### ***Features of a property transaction involving identity fraud***

A typical mortgage fraud transaction will begin with the fraudster approaching a lender (often a 2<sup>nd</sup> tier lender such as a finance company), and offering a property as security for the loan. They will be able to produce high quality forgeries of the true owner's identity documents, as well as bank statements and utilities bills. In some cases, the fraudster will claim that the title deeds to the property have been lost, and produce a set of certified copies which have also been forged.

The fraudulent borrower then meets with the lender's solicitors to sign the mortgage and relevant documents (usually this will be the first and only time that the solicitors meet the fraudster in person). The loan funds will be transferred to the solicitors, and the solicitors then pay the funds to the fraudster.

Usually, the fraudster makes a couple of loan repayments, then disappears. The fraud comes to light, the mortgage is set aside, and the lender seeks to recover its loss from the solicitors. The usual allegation is that the solicitors were negligent in failing to verify the borrower's identity and/or failed to properly investigate the title to the property.

### ***Applicable legal principles***

There have been 2 recent decisions dealing with solicitors' duties in identity fraud cases in property transactions: *Yip Kin Kwan Kenneth v Rich Well Finance Ltd* [2020] HKCFI 456 and *Gain Global Corporation Limited v Fongs (a firm)* [2024] HKCFI 894.

### **Scope of solicitor's duties**

Both of these cases involved retainers which did not include express instructions for the solicitors to verify the borrower's identity. The decisions in both cases reinforced the following established principles:

- The extent of a solicitor's duties will depend on the terms and limits of the solicitor's retainer. Any implied duty of care must relate to what the solicitor is instructed to do.

- Clear terms would be required if commercial institutions such as banks wished to impose an absolute liability on members of a profession.
- A solicitor is not expected to advise upon the commercial good sense of a business proposition.
- Risks are always associated with entering into a mortgage transaction, and the lender would and should have made provision for such risk.

## Solicitors' duty to investigate title

In *Rich Well Finance*, the Court accepted that it was not possible for the solicitors to investigate title since the lender knew that it was a 2<sup>nd</sup> mortgage, and the title deeds were in possession of the 1<sup>st</sup> mortgagee.

In *Gain Global*, the solicitors were provided with purportedly certified true copies of the title deeds, on the pretext that the originals had been lost. The solicitors raised concerns about this, but the lender dismissed their concerns and went ahead with the loan.

In both cases the Court found there was no breach of duty by the solicitors:

- The solicitors never assumed any absolute or unqualified obligations to ensure or warrant that the lender could obtain a good title under the mortgage. No words to that effect were included in the instructions. There was no undertaking by the solicitors to insure against any identity fraud.
- There is a critical difference between an instruction to check that a registered owner has good title to the property versus an instruction to be satisfied that the person with whom the client is dealing has good title to the property.

## Solicitors' duty to verify identity

In both *Rich Well Finance* and *Gain Global*, it was found that the solicitors were not under any duty to verify the identity of the borrower or to satisfy themselves that the borrower was the registered owner of the property, since this was not specified in the instruction letters.

In *Rich Well Finance*, the Court also found that the lender had failed to prove that the solicitors had breached their duty to exercise reasonable care and skill as alleged or at all.

In particular, it was found that:

- It was reasonable for the solicitors' firm's conveyancing clerk to verify the identity of the borrower by checking the HKID card.
- The lender was in a much better position than the solicitors to form a judgment as to the borrower's trustworthiness. It was reasonable for the solicitors to assume that the lender had taken steps to verify the identity of the borrower before instructing the solicitors.
- It is wrong and unfair for the lender to try to highlight some differences in the signatures in isolation since:
  - conveyancing clerks are not experts in examining signatures;
  - the signatory was present and his identity had already been verified to the clerk's satisfaction;
  - no signatures by the same person are identical; and
  - comparing signatures would unlikely be an effective means to detect forgery - the forger will try to imitate the genuine signature.

The above was adopted by the Court in *Gain Global*. The Court also found that as long as the identification documents produced by the borrower are on their face genuine and without any apparent irregularities, it is unnecessary for the solicitors to go and search for other independent documents to verify the borrower's identity.

In both cases, the Court refused to allow the lenders to effectively pass the risk of identity fraud on to their solicitors. These decisions should not, however, lead to complacency on the part of solicitors handling property transactions. Below are some suggestions for minimising the risk of a claim arising from identity fraud.

## ***Reducing the risk of identity fraud – key takeaways***

1. **There should be an engagement letter setting out the terms of the retainer** - see RME Bulletin No. 2 on Retainer Letter (see Law Society Circular no. 22-460 published in July 2022).
2. **Pay attention to the precise wording of the engagement letter** - even less onerous obligations such as 'investigating title' should only be included if the extent of any such investigation is clear.
3. **Do not accept wording which has the effect of making you guarantee the title to the property and/or the identity of the borrower.**
4. **Instruct all property team members to keep attendance notes of all substantive telephone calls and meetings with the client** – particularly for instructions received and advice provided. These can be of vital importance if it is necessary to defend against a claim. See also RME Bulletin No. 1 on Importance of Attendance Notes (see Law Society Circular 22-239 published in April 2022).
5. **Take particular care when presented with certified copies of documents of title** - purportedly “lost” title documents are a major red flag, so take extra steps to ensure that the certified copies are genuine. Ensure that you inform the client that the title documents are not originals, and advise them of the risk of fraud.
6. **Provide internal written guidelines for property team members to follow on identification of clients / mortgagors** - these guidelines should cover verifying the identity of individuals, including procedures for checking their HKID and the security features of the HKID to ensure that they are genuine, comparing signatures of borrowers / mortgagees with documents obtained from the Land Registry, and steps to be taken when presented with certified copies of title deeds. Property teams should also be familiar with the guidance notes for HKID cards issued by the Immigration Department.
7. **Ensure that unqualified staff involved in handling property matters are always supervised by a legally qualified person with conveyancing experience.**
8. **Establish and maintain a clear reporting line** - case handlers should know who they can speak with if there are any issues or any suspicious red flags in the transaction.

9. **Be wary of unqualified staff who are too close to the staff of lender clients** – as this can lead to the risk of deliberately ignoring risks or even collusion in wrongdoing.
10. **Provide regular training for staff** - in particular, training to reinforce awareness of risks and proper examination of identity documents.
11. **Keep staff informed / updated on latest fraud claims and Law Society Circulars on suspicious transactions / individuals.**