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Forged Mortgages and Queensland's Careless Mortgagee Exception to Indefeasibility

Introduction

The Supreme Court of Queensland has recently considered the position of a mortgagee who failed to make appropriate identity checks when obtaining its securities. In *Commonwealth Bank of Australia v Perrin* [2011] QSC 274, McMurdo J considers the validity of the documentation relied on by the bank and the operation of the exception to indefeasibility known as the 'careless mortgagee' exception which provides a defence to a claim for possession or sale by a mortgagee. While the exception has applied in Queensland since 2006, this is the first time a case relying on it has come before the court.

The legislation

Section 185 (1A) of the *Land Title Act 1994* (Qld) provides that a mortgagee does not obtain the benefit of indefeasibility if the mortgagee failed to comply with s 11A (2) of the *Land Title Act 1974* (Qld) and the mortgage was executed by someone other than 'the person who was, or who was about to become, the registered proprietor of the lot or the interest in a lot for which the instrument was registered.' Section 11A (2) requires the mortgagee take reasonable steps prior to lodgement, to ensure the person who has executed the mortgage as mortgagor is identical with the person who is or is about to become the registered proprietor of the land (or the interest in it). While not the only means of satisfying the obligation, a mortgagee takes reasonable steps to confirm identity if it complies with the practices included in the Land Title Practice Manual. This generally reflects the '100 points of identification' requirements of the *Financial Transaction Reports Act 1988* (Cth) and the *Financial Transaction Reports Regulations 1990* (Cth). However, depending on the circumstances, further checks may be required in order to satisfy the obligation to take reasonable steps. When dealing with an existing customer, the mortgagee must ensure the person giving the mortgage is in fact the existing customer. Similar obligations to confirm identity apply in the case of an amendment of mortgage (see the amendments to s11A in 2010) and to a mortgage transferee under s 11B.

The provisions catch the conduct of a mortgagee in those forgery cases where the mortgagee's title is not tainted by fraud but where the mortgagee did not undertake adequate checks of identity. While placing the risk of forgery firmly on the shoulders of the person who is arguably most able to avoid it, the effect is to reduce the financial burden on the State.

Facts

In *Commonwealth Bank of Australia v Perrin* [2011] QSC 274, a husband obtained loans in excess of \$10 million from the Commonwealth Bank. As security, the bank obtained what it thought was a guarantee executed by his wife and mortgages over the family home owned solely by the wife. When the husband's financial position deteriorated (he was subsequently declared bankrupt), the bank sought to enforce its security. The wife claimed the guarantee and mortgages were forgeries and that she had no knowledge of these financial arrangements.

The bank's arguments

The bank argued that the wife did sign the documents or alternatively if not signed by her; they were binding on her because they were signed by the husband either with her express or implied authority or because she subsequently ratified them. If these arguments failed, the bank sought to establish an equitable mortgage in its favour by the deposit of the certificate of title. Lastly, the bank argued in the alternative, that if it was established that the exception to indefeasibility applied, that s187 of the *Land Title Act 1994* (Qld) gave the court the power when removing the mortgages, to ‘make the order it considers just.’ The bank argued that an order for removal of the mortgages should be accompanied by an order for contribution to the outstanding debt by the wife on the basis that she was partly to blame for the fraud.

Given the arguments raised by the bank, the focus of the judgment is on the facts surrounding execution and the authority of the husband, the bank conceding that it did not take reasonable steps to ascertain the identity of the person signing as required by s 11 A of the *Land Title Act 1994* (Qld).

Were the signatures genuine?

McMurdo J, relying on s 59 of the *Evidence Act 1977* (Qld), compared the disputed signatures with specimen signatures known to be genuine. The court was assisted in its decision by document examiners who prepared charts showing the variations in the specimen signatures which might naturally occur. To ensure the sample was representative, it included some signatures produced by the bank. The court took into account the fact that signatures are likely to change over time and as a result of the circumstances in which they are given (at [86]).

The court also considered the reasons why the husband might forge the wife’s signature rather than seek her agreement to the transactions. These included the difficulties being experienced within the marriage, financial pressure on the husband and his likely desire to hide the need to borrow such a large sum which would have concerned her given their apparent wealth. The court was not persuaded by the bank’s attempts to show that the wife knew of the transactions. The conclusion reached was that on the balance of probabilities the relevant signatures were not those of the wife (at [103]). This conclusion was assisted by a finding that the signatures of the solicitor (the husband’s brother) apparently witnessing the wife’s signature had also been forged (at [104]).

Did the husband have express or implied authority to sign?

The bank’s argument that the documents had been executed by the husband with the express authority of the wife pursuant to a power of attorney failed. It was accepted that it was more probable than not that a power of attorney prepared by solicitors some years before had not been signed by the wife. It was found that a copy of a power of attorney apparently signed by the wife was a fabrication of the husband. He had created it after he obtained the file relating to the preparation of wills and powers of attorney from the solicitors acting on the couple’s behalf in relation to that matter (at [67] and [116]).

A further argument of the husband’s implied authority to incur financial liability and to deal with the wife’s property based on the nature of the relationship between them was also unsuccessful. The husband was a well educated business person who in managing their financial affairs had accumulated significant wealth while his wife had relatively less education and who upon becoming a mother had not engaged in business. While it seems clear the husband managed the business interests of the family, this did not translate into authority to deal with the family home owned by the wife and to incur significant personal

liability on her behalf. The court did not accept that the wife would have signed the bank's documents if presented to her and took the view that even if that had been the case, 'it does not follow that absent that agreement, he was impliedly authorised to effect them in her name.' (at [136])

Given there was no express or implied authority for the husband to enter the transactions, the court was also asked to consider if the transactions were binding on the wife by her subsequent ratification. The bank based its argument on the wife's delay in notifying the bank of the forgeries and by her movement of money through various bank accounts at about the time the transactions became apparent to her. The court found her delay in notifying the bank might be explained in a number of ways including the need to obtain legal advice. The argument that an innocent person might by ratification become bound by a forgery was found to be contrary to authority (at [144]). His Honour prefers the view that this is the case because a forger is not an agent for his or her victim. In any event, on these facts there was no adoption of the transactions by the wife who would gain nothing by being bound by them but would incur substantial personal liability. In appropriate circumstances an estoppel might arise but no such argument seems available here and was not in fact raised by the bank.

No Equitable mortgage

The court found the registered mortgages did not have the benefit of indefeasibility and then went on to consider the claim that the bank was entitled to an equitable mortgage by deposit of the certificate of title. Section 75 of the *Land Title Act 1974* (Qld) confirms an equitable mortgage of Torrens land can be created in this way. However, as the certificate of title was delivered to the bank without the wife's authority, no equitable mortgage was created.

'Just' orders

Having failed to establish the wife was bound by the documents, the bank claimed that it was entitled to some payment from the wife pursuant to s 187 of the *Land Title Act 1974* (Qld). Where indefeasibility is lost pursuant to, inter alia, s 185(1A) then s 187 gives the Supreme Court power to 'make the order it considers just.' Examples of the orders that might be made are outlined in s 187 (2) and include correcting the register. Given the wife's signatures on the guarantee and mortgages were forged and indefeasibility was lost, it would seem the mortgages should be removed from the title. However, the bank argued that the mortgages should only be removed from the register if the wife paid half the husband's debt because she contributed to the fraud by allowing the release of the certificate of title from the solicitor holding it on her behalf for safe keeping. This argument could not succeed for 2 reasons. Firstly, the husband was not authorised to remove the certificate of title to deal with it as he did (at [156]). Secondly, s 187 does not give the court such a discretion. His Honour said (at [159]):

Thus the power to make "the order it considers just" does not empower the court to override existing entitlements and obligations and, in particular, to affect the interests of a registered proprietor (in this case the defendant) by encumbering her title in a way for which there is no legal basis. Rather it is a power which is to be exercised only in accordance with the respective legal positions of the parties which will be affected by the order. In the present case, the bank has no indefeasible title. And it has no title otherwise, because there was no transaction between it and the defendant. There is no power to make the order in the terms for which the bank contends, which would effectively create a charge over the defendant's land.

A lesson for lenders

The bank conceded it had not verified identity and as a result the focus of the decision is on an assessment of the facts surrounding execution of the documents and whether the signatures were genuine or not. This case highlights the enormous impact the 'careless mortgagee' exception to indefeasibility will have on lenders who fail to adequately identify their customers. While a mortgagee may not be a party to the fraud, the benefits of registration of a mortgage may be lost through a failure to identify.

Lenders must be meticulous in confirming identity to ensure compliance with s 11A of the *Land Title Act 1974* (Qld) when entering into mortgages. This should be the case regardless of the stature of the client they believe they are dealing with. The case certainly highlights the dire consequences of a failure to comply; that is, the loss of the benefits of registration and no claim for compensation from the State.

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