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Second interim report of the Conveyancing Practices Task Force

FOR DISCUSSION AND COMMENT

The Law Society of British Columbia

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INTRODUCTION

On June 29, 2002 the Benchers of the Law Society appointed the Conveyancing Practices Task Force to explore and report out on current conveyancing practice issues. The review followed the disclosure of certain practice irregularities in real estate transactions conducted by Vancouver solicitor Martin Wirick in connection with one of his vendor clients. The Task Force began work to address concerns that new steps may be needed to prevent similar problems in the profession in the future.

The Task Force is keenly aware of the need for change in conveyance practice to restore public and professional confidence in lawyers' undertakings and in the integrity of the lawyers in real estate transactions. This remains a driving force behind our work.

On August 6, 2002, the Task Force published its first interim report, which drew considerable interest and reaction from within the profession, the financial community and the public. That reports sets out full background to the work of the Task Force and is available in the Resource Library/Reports section of the Law Society website at www.lawsociety.bc.ca.

Since the publication of its initial report, the Task Force has met with various interested groups, including the CBA Real Property Sections, representatives of the lending community and representatives of the Society of Notaries Public.

As well, the President and senior staff of the Law Society, with encouragement from the Task Force, have lobbied for the prompt proclamation of section 13 of the BC *Cost of Consumer Credit Disclosure Act*. This section imposes an obligation on financial institutions to provide a discharge of mortgage within 30 days of repayment. The government has also been lobbied by the financial community to delay implementation of this section until further study has been done.

In the result, the proposed effective date of the legislative change has been postponed from December 1, 2002 to some future date to be determined. It should be evident that any incentive to prompt processing of discharges of mortgage will benefit the public.

This second interim report describes the work undertaken by the Task Force in the past four months, taking into account our various consultations. It provides an update on initiatives introduced in the first report and describes new initiatives considered by the Task Force. The Task Force looks forward to receiving the views of the profession and interested members of the public on this report.

THE FIRST INTERIM REPORT: RESPONSES AND REVIEW OF INITIATIVES

Many members of the legal profession provided feedback to the Task Force on its first interim report. The Task Force is indebted to those who took time to reduce to writing their concerns, suggestions and possible solutions to the problems identified.

A common theme was evident in the comments of many lawyers – antipathy to the two-cheque system that was proposed in the first interim report. While there were different reasons for that view and no single overarching criticism, it is fair to say that supporters of the two-cheque system were few.

At the end of the day, the lack of lawyer support for the two-cheque system spelled its demise and the Task Force decided against pursuing that initiative. The Task Force thanks the Vancouver Real Property of the CBA, with the assistance of the Real Estate Contract Committee, chaired by Ed Wilson, for having crafted contract language and undertakings that would have allowed for implementation of a two-cheque system.

A second theme emerged from our consultations with the profession. BC lawyers stressed as paramount the need to restore confidence in the integrity of solicitors' undertakings. This view was shared, to some extent at least, by representatives of the lending community with whom the Task Force has had ongoing discussions. Without doubt, the role of the solicitor's undertaking is extremely important in conveyancing transactions, so there is need for certainty in respect of the effectiveness and reliability of those undertakings. In recognition of this, the Task Force has recommended both new conveyancing reforms and a modified form of fidelity insurance, or innocent party insurance coverage, as it is called in this report.

A troubling aspect of providing unequivocal support for solicitors' undertakings is that there is a risk of serious abuse, such as a fraudulent scheme, that is of unmanageable magnitude. The legal profession should contemplate limits on the responsibility of Law Society in standing behind the financial consequences of breaches of undertakings. With the exception of the claims pending against Mr. Wirick, there is no historical basis to anticipate unmanageable losses, but it is nevertheless prudent to foresee such a possibility. For that reason, the innocent party insurance program described in this second report provides limits on coverage.

For the same reason, the Benchers might wish to consider re-establishing limits on payments from the Special Compensation Fund.

If the Law Society were to undertake unlimited responsibility for trust defalcations generally (albeit subject to a discretion), they should do so deliberately and not by default simply because of the approach taken on the Wirick claims. The Task Force understands that removing Special Compensation Fund limits was particular to the Wirick matters and not intended to change the general approach to claims.

While many within the profession expressed views on the Task Force's first interim report, there was also a significant response from the media and general public. Public criticism was directed at the Task Force's proposal for a new fee on real estate transactions, with proceeds being used to underwrite, at least in part, any approved claims arising from the practice of Martin Wirick.

In the view of the Task Force, any suggestion that the proceeds of fidelity insurance be used to fund past financial losses, such as any approved claims arising from the Martin Wirick transactions, must be abandoned. While it is true that lawyers have a limited ability to raise funds save from their clients, use of a transaction fee to fund past losses will never achieve the degree of understanding necessary to make it palatable to the public at large. The extent and level of rhetoric that flowed from the initial Task Force report verifies that the Law Society's ability to garner support for a transaction-based fee to fund past losses is not possible.

The Benchers are currently examining alternative funding sources for the Wirick claims. One likely approach to is authorize an assessment of BC lawyers, to be paid over a period of time. This is a matter exclusively within the purview of the Benchers. and it is not within the Task Force's mandate to consider further.

NEW PRACTICE INITIATIVES

A 48-hour notification of mortgage repayment *(Transparency Response)*

The Task Force recommends a universal practice change that can be characterized as a "transparency response." This initiative would ensure prompt verification by a vendor's solicitor to the purchaser's solicitor of a mortgage repayment in a real estate transaction, which would also be subject to independent third-party verification. A subcommittee of the Vancouver Real Property Section has done considerable work to craft documents that formalize the practice changes necessary to implement this regime. These will be considered by the Section at its meeting on January 6, 2003.

In the view of the Task Force, the transparency response has much to recommend it and should be adopted on a province-wide basis to respond to perceived deficiencies in conveyancing practices.

In its simplest terms, the transparency response requires a vendor's solicitor to provide to a purchaser's solicitor, within 48 hours of the completion of a transaction, evidence that the vendor's solicitor has repaid existing encumbrances on title. This evidence will take the form of photocopies of correspondence that accompanied the repayment, copies of cheques representing the repayment proceeds and a copy of the existing chargeholder's repayment statement.

In our discussions with the lending community, it has been acknowledged that the participation of financial institutions would go a significant distance to validate the accuracy of repayment information. One proposal is to develop a protocol under which a financial institution would acknowledge receipt of the funds representing the repayment.

While the financial institutions have not yet committed to providing this acknowledgement, and further discussions will ensue, their initial reaction is positive. For financial institutions to acknowledge receipt of a mortgage repayment would greatly enhance the transparency response. An additional step would be for a vendor's lawyer to provide the name of a person within the financial institution who could be contacted by the purchaser's lawyer to verify the accuracy of the repayment information and documentation provided by the vendor's lawyer.

The Task Force has canvassed concerns about breach of confidentiality if the vendor's lawyer were to share with the purchaser's lawyer mortgage repayment information. (Similar confidentiality concerns were raised at an earlier stage of the Task Force's work when it was proposed that a purchaser's lawyer might repay the vendor's mortgage debt directly to the relevant financial institution.)

To address the concerns, it is anticipated that the purchaser's lawyer will seek the purchaser's permission to receive verification of the repayment of the existing mortgage, without an obligation for the lawyer to disclose that information to the

purchaser. The amount of the vendor's indebtedness is not information of use to a purchaser, and this is particularly true when the transaction has completed. It is thus expected that, in virtually all circumstances, purchasers' solicitors should be able to seek and obtain such consent from their clients.

To the extent that it is necessary for the Law Society to become engaged in the widespread acceptance of this transparency response within the profession, we recommend that all necessary steps be taken. The Task Force notes that the adoption of the transparency response by the CBA Real Property Sections across BC will provide the necessary momentum to have the new practice adopted province-wide at the earliest possible date. The Task Force will continue to monitor these initiatives and provide further reports as necessary.

Reporting the failure to provide mortgage discharges *(The 30-30 Rule)*

The Task Force also recommends that the Law Society adopt, for a limited period, a rule we refer to as the "30-30 Rule." In its simplest terms, the proposed rule would allow 30 days for a financial institution to provide a mortgage discharge and a further 30 days for the solicitor receiving the discharge to process it through the Land Title Office. If the mortgage had not been discharged in the land title system within the total of the 60 days provided by the 30-30 Rule, the BC lawyer responsible for receiving the discharge would be required to advise the Law Society's Corporate Secretary that the institution had failed to provide a discharge and that the discharge remained outstanding. Similarly, a lawyer would be required to advise the Corporate Secretary if another lawyer in the transaction had not provided discharge particulars of a mortgage in that period.

For example, if there was no mortgage discharge in a real estate transaction within the cumulative 60-day period, two separate reports would be sent by lawyers to the Law Society. The vendor's lawyer would send a report to indicate that he or she had not received the requisite discharge of mortgage from the financial institution. The purchaser's lawyer would send a separate report indicating that he or she had not received discharge particulars from the vendor's lawyer.

The primary purpose of this initiative is to build a database of information about the response time in the financial industry in processing mortgage discharges. It is hoped that these reports will flag for the Law Society if there are particular financial institutions that appear unable to meet their obligations within the specified timeframe. In meetings with the Task Force, representatives of the financial institutions have expressed a willingness to expedite mortgage discharges with the goal of preventing abuses and problems in conveyances. They also appear prepared to work out a protocol whereby a responsible contact within each institution would be available to address problems arising from delays in mortgage discharges.

The second purpose of the reporting rule is to discover if there are situations that require attention or intervention from the Law Society. The Task Force notes, for

example, that information provided under such a rule, together with the cooperation of financial institutions, could have provided an earlier warning of problems relating to the practice of Mr. Wirick.

The Task Force emphasizes, however, that adverse inferences will not be drawn against lawyers from the reports generated under the 30-30 rule, unless there is evidence of defalcation or breach of undertaking. No stigma attaches to a particular lawyer who has simply been unable to obtain a discharge of mortgage from a financial institution following repayment of the debt.

The Society of Notaries Public has now adopted a similar reporting requirement for notaries in BC, expected to take effect January 1, 2003. The Task Force recommends that the Law Society and the Society of Notaries Public will share information under their respective rules.

The Task Force proposes to bring forward a new rule or rules for Bencher consideration in February, 2003, with a recommendation for early implementation.

FINANCIAL PROTECTION INITIATIVE: INNOCENT PARTY INSURANCE COVERAGE

The Task Force recommends that the Law Society adopt a program of innocent party insurance coverage. This initiative was introduced in our first interim report and approved in principle by the Benchers in September, 2002. The Task Force has since begun work on fleshing out the details and options for further consideration.

At the outset, we note that this insurance program contemplates coverage *on a go-forward basis only*. As earlier noted, it is no longer intended that the premium proceeds from this insurance would be used to fund past losses, such as any approved claims arising from the practice of former lawyer Martin Wirick.

Moreover, while the insurance program was initially contemplated to cover losses arising from breaches of lawyers' undertakings, the Task Force now recommends that it cover losses arising from any trust defalcations by a lawyer.

A number of aspects of this insurance coverage require further investigation and actuarial analysis, and the Benchers will need to make various policy choices for the program to go forward.

It is worth noting that, over time and with the concurrence of the Attorney General, innocent party insurance coverage could replace the Special Compensation Fund. This would have the advantage of replacing the present *discretion* that underlies Special Compensation Fund payments with a contract-based *entitlement* to compensation for losses flowing from lawyers' defalcations. This entitlement would be subject to certain limits and publicized so that members of the public involved in trust transactions would be entitled to make alternative arrangements in those circumstances where the limits might be exceeded.

The Task Force is initially considering innocent party insurance coverage of $1 million per transaction, with an annual aggregate of $10-15 million per lawyer. We note that, had a program with those limits been in place previously, it would have responded to all Special Compensation Fund claims over the past 30 years, with the exception of the claims arising from the practice of the Martin Wirick. It is the view of the Task Force that those insurance limits are adequate to protect the public interest. Moreover, the program can be expanded and the limits changed over time, in accordance with claims experience and actuarial projections.

There are essentially three options for funding the insurance program: 1) a transaction-based approach, 2) a general premium approach, or 3) a combination of the two.

The Task Force unanimously recommends the adoption of a blended premium, being a combination of:

- a general insurance levy assessed against all practising lawyers in BC; and

- a fee paid by law firms with respect to each trust account (or ledger within a pooled trust account) opened within the firm for a client respecting a specific legal transaction or other legal matter.

It is expected that there would be a base level trust deposit (perhaps $5,000 to $10,000) before a client matter would become subject to the transaction fee. In addition, it is proposed to exempt from the fee all matters in which the trust account is used only for the payment or collection of retainers.

It should be clear that the Task Force intends that *only one fee* would be levied on each individual trust account (or trust ledger within a pooled trust account) opened for a client respecting a particular legal transaction or other legal matter. *It is not intended to impose a fee on each trust cheque written or each deposit made to trust for the client.* For example, a single conveyance for which there are trust deposits from the client and from a mortgagee and also payment to the vendor's solicitor, real estate agencies and the law firm (for fees and disbursements) would attract a single fee.

There is as yet no statistical information on which to establish the appropriate amount for the fee. At this early stage, the Task Force estimates that a fee in the order of $10 per client matter would generate annual revenues of $3,000,000.

While in its first interim report the Task Force projected a transaction fee ranging from $30-40 per conveyancing trust transaction, the new projection should allow for a much lower transaction fee. This is possible in part by the general insurance premium blend, and the fact that the new trust transaction fee would be based on a significantly broader array of transactions. (The original recommendation was that the fee confined in its scope to real estate transactions.)

The Task Force has directed Law Society staff to gather actuarial information to help determine the amount of a blended premium, both the general component and the transaction fee component. This includes gathering statistical information on the numbers of trust transactions likely to be affected and actuarial information with respect to the appropriate level of general premiums. The Task Force will strive to recommend a premium that minimizes the burden on lawyers and their clients, while at the same time providing an appropriate level of insurance coverage.

In addition to this analysis, there is work to be done in crafting rules and regulations on the details of this initiative.

As a result of work still to be done, the insurance will not come into effect on January 1, 2003 as initially contemplated.

No hiatus in protection for the public will result from this delay. The Special Compensation Fund continues to respond to lawyers' defalcations, and will continue

to do so in the foreseeable future while the alternative insurance based program is developed.

The Benchers have resolved to increase the Special Compensation Fund assessment from $250 in 2002 to $600 in 2003, thereby generating considerable additional revenues for the Fund. As well, the insurance coverage for the Special Compensation Fund has been renewed by the insurer for 2003.

NEXT STEPS

At their meeting on December 6, 2002, the Benchers approved in principle the Task Force recommendation of a 30-30 rule, as set out in this report, and have approved the Task Force continuing work on the other initiatives and undertaking further consultations.

As a result, the Task Force will request and review new Law Society Rules to implement the 30-30 rule, for consideration by the Benchers at their meeting in February, 2003. The Task Force will also continue work on its other initiatives, that is, a requirement for vendors' lawyers to provide prompt verification of mortgage repayment (the transparency response) and an innocent party insurance program. In furtherance of these initiatives, we will continue to monitor work within the CBA Real Property Sections and to meet with both the Notaries and the financial institutions.

As already noted, the Task Force is extremely grateful for the many thoughtful responses to its first interim report – from individual lawyers, law firms and bar associations, CBA sections and other groups of lawyers, as well as from the financial community. It is important for that feedback to continue.

In this spirit, the Task Force is publishing this second interim report, with the approval of the Benchers, and welcomes comment from those within the legal profession, from financial institutions and from other interested members of the public. Please send comments to:

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