

Managing the risk of Seller fraud in the aftermath of Dreamvar

It's nearly five years since the Court of Appeal handed down judgment in what has become commonly referred to as "Dreamvar". This guidance explores the impact of the Dreamvar decision using real life "imposter" scenarios which have resulted in claims against conveyancers acting for both Sellers and Buyers and seeks to draw out potentially useful "take-aways" for practitioners.

Dreamvar - a quick recap

The basic facts are well known: the Court examined two separate residential conveyancing transactions dating from 2013 and 2014 respectively, where the Buyers' solicitors forwarded completion monies to the Sellers' solicitors who in each case were unwittingly acting for imposters. The completion monies were paid away to the imposters and never recovered.

Strong Protection for innocent purchasers

The Dreamvar decision confirmed that, in an imposter situation where the Law Society Code for Completion by Post (the "Code") applies, the Buyers have a claim in breach of trust against both their own solicitors and the solicitors for the purported Sellers. Unless the Buyer is, say, a financial institution, it can be pretty sure neither solicitor will be granted s61 relief. Depending on the facts, Buyers may also have claims in contract and tort against their own solicitors and a claim in respect of the Sellers' solicitors' breach of undertaking. Accordingly, Buyers have extremely strong protection if they are the victims of imposter fraud.

Seller's solicitors at risk of claims, but purchasers' solicitors may be liable for % contribution

But what about the solicitors? Apart from confirming the position about the absence of a duty of care, Dreamvar did not expressly deal with the position as between the solicitors. However, the clear implication of the decision is that the Buyers' solicitors will have direct claims against the Sellers' solicitors pursuant to the Code in breach of undertaking, and, given the contractual/agency arrangements involved in the Code, possibly also in breach of fiduciary duty.

We are yet to see what impact the [Harcus Sinclair LLP & Anor v Your Lawyers Ltd \[2021\] UKSC 32](#) decision will have on breach of undertakings claims under the Code.

Should the need arise, where both sets of solicitors are liable to the Buyers for the same damage, there can also be contribution claims between them, but these are most likely to come into play if the Code does not apply. Even where the Code does apply, there may still be reasons for the "innocent" Buyer's solicitors to contribute to a settlement:

- > because Dreamvar did not deal expressly with the position as between Solicitors, and given the dearth of on-point case law, there remains some inherent uncertainty.
- > where there exists doubt as to the terms on which completion monies were held.
- > where the Buyer's solicitors' own transaction file is open to criticism (e.g. if it reveals weak Client ID or AML processes).
- > where, commercially and pragmatically, a modest contribution by the Buyer's solicitor is all that is standing in the way of a prompt settlement.

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The implications of Dreamvar in practice: 5 seller fraud case-studies

Sale & Purchase: Seller's solicitors in breach of the Code

Case study #1: A Dreamvar fairy tale ending (for the Buyers and their solicitors)

Solicitors acted for the would-be Buyers of a £750,000 London property in October 2019. The 2019 Code applied. Completion monies were paid over to the Seller's solicitors, and a signed Transfer received.

However, the Land Registry cancelled the application for registration of the purchase and of the lender's charge on the grounds it was unable to verify the ID evidence lodged in respect of the Sellers.

It very quickly became clear that the "Sellers" were not who they had purported to be (in fact it transpired that the true owners were a married couple -a man and a woman- who were both foreign nationals, whereas the imposters' ID consisted of British passports for two men).

Pursuant to Dreamvar:

- a. Both Buyers' and Sellers' solicitors were in breach of trust to the Buyers.
- b. Neither solicitors' firm was likely to be awarded s 61 relief, given that the Buyers were individuals (without the benefit of any insurance) and whose life savings had gone into the purchase.
- c. The Sellers' solicitors were in breach of undertaking given to the Buyer's solicitors.

The deficit in client account was remedied, and happily, a complete recovery was obtained from the Sellers' solicitors, who conceded breach of undertaking pursuant to the Code. The recovery claim had also raised various other issues relevant to contribution, but these were not needed given the concession on the undertaking.

Practical take-aways

- **Protect yourself from arguments that the Code does not apply: do not accept 'at the buyer's risk' wording in the TA13.** CQS accredited practitioners must agree to follow the Conveyancing Protocol which automatically implies use of the Code. Conveyancers will also know that the Completion Information and Requisitions on Title form (Form TA13) states: "We wish to complete through the post, in accordance with the Law Society's Code for Completion by Post 2019 (the Code)" It then asks: "Please confirm that: (a) You undertake to adopt the Code".

In this case, the Sellers' solicitors had answered: "Confirmed but at the Buyer's risk".

The Buyers' solicitors had asked for a completed TA13 with those words removed. This was helpful in eliminating any argument that the Sellers' solicitors might have sought to raise that the Code did not apply.

- **Be aware of potential additional heads of loss for your client:**

Lender redemption penalties: The Buyers' solicitors having replenished client account, the Buyers' liability to the lender was also settled. However, the lender then sought to impose a (hefty) redemption penalty. Not only was this somewhat harsh given that their borrowers had been the innocent victims of fraud, but, in our view also wrong: could there be said to be "redemption" of a mortgage which had effectively never been "completed"? The penalty was dropped.

Mortgage broker commission: The lender also clawed back the commission it had paid to the mortgage broker. The broker then sought this "lost commission" from the Buyers' solicitors. This also got short shrift. There had been a fraud. The transaction ought never to have gone ahead. The broker had suffered no loss in having to return commission to which it had never properly been entitled.

SDLT: HMRC was slow to accept that there was no completion such that no SDLT was due. But they accepted the position in the end.

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Sale & Purchase: Seller's solicitors in breach of the Code, but their PII insurer declines cover

Case study #2: The Dreamvar nightmare scenario (for the Buyers' solicitor)

Imagine you receive instructions from Buyers of a £250,000 Buy-to-Let property. The 2019 Code applies. You pay the completion monies over to the Seller's solicitors. But your clients discover (for example, through an enquiry with the former owner) that he hadn't given anyone instructions to sell his property. It transpires the completion monies were paid away to an imposter and there was no genuine completion.

However, then the Seller's solicitors' Professional Indemnity Insurers decline cover.

Practical take-aways

- **Include an assessment of the Seller's solicitor in your risk assessment.** If you are dealing with a solicitor who turns out to have been dishonest, any rights of recovery against that solicitor may be of limited or no value because their insurer may be entitled to refuse to indemnify that solicitor. Other than where the solicitor involved is a sole practitioner (in which case extra vigilance might be sensible) it would be highly unusual to have a situation where there are no other honest partners or honest LLP members in the Sellers' solicitor's practice entitled to take an indemnity, but it's not unknown.

Where there's no one at the Sellers' solicitors entitled to an indemnity from their insurer, then unless the principals of the Sellers' solicitors have significant personal resources (e.g. unencumbered property), the Buyers' solicitors and their insurers will have to pay up.

Do not expect the Compensation Fund to step in: it is not there to allow solicitors to effect a recovery in respect of their own liability to clients.

Where the Seller's solicitor is not one you are familiar with, particularly if they are a sole practitioner, it is important to be alert to any signs that might indicate they are not undertaking their responsibilities with proper professionalism. Train staff regarding warning signs to look out for.

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Re-mortgage: Imposter borrowers

Case study #3: Variations on a Dreamvar theme (imposter borrowers)

In our experience, fraudulent re-mortgages are being treated as analogous to the **Dreamvar** situation.

Solicitors act for a borrower taking out a bridging loan. The re-mortgage completes, and the proceeds are paid away to the borrower client. It transpires that the client was an imposter, and, inevitably, because the money has gone to a fraudster, there is an immediate default on the bridging loan repayments. The true registered proprietor discovers the fraud only when the lender institutes possession proceedings.

The understandably outraged true owner halts the possession proceedings and successfully applies to HMLR to have the register rectified to remove the lender's charge. The outraged lender then successfully seeks an indemnity from HMLR for the loss of its charge. HMLR, on behalf of an outraged public, then casts around for someone to sue to recover its outlay.

Schedule 8 to the Land Registration Act 2002 allows the registrar to enforce any right of action that a claimant would have been entitled to enforce had the indemnity not been paid or that a person in whose favour the register has been rectified could have enforced if the register had not been rectified.

In this scenario, HMLR can stand in the shoes of the lender and bring any claim the lender would have been able to pursue had the indemnity not been paid out. So, HMLR brings a claim against the solicitors for the imposter borrower, on the basis they are in breach of trust for payment away of the re-mortgage proceeds otherwise than for a genuine re-mortgage.

There is no Code here and leaving aside possible technical direct causes of action in agency and breach of fiduciary duty which may apply, there is no obvious direct claim as between the purported Borrowers' solicitors and those acting for the lender. However, there may be grounds for the Borrowers' solicitors to bring a contribution claim against the lenders' solicitors on the basis they are each liable to the lender/HMLR for the same damage i.e. the damage arising from the breach of trust.

The amount of the contribution or indemnity in a contribution claim is determined by what the court considers just and equitable having regard to the extent of that person's responsibility for the damage in question, encompassing an examination of blameworthiness, and causal potency.

This is when attention will focus on both solicitors' transaction files: their respective duties and attempts to ascertain and verify their client's identity; their AML and risk assessment processes; and what opportunities each had to notice, report, and/or to advise about any 'red flags'.

Practical take-aways

- **The Code does not always apply**
- **Be aware - it is not always the Seller's solicitor who is best placed to detect fraud.** The judges in Dreamvar commented that it will generally be the Sellers' solicitors (and therefore by analogy in re-mortgage case, the Borrower's solicitors) who are best placed to detect fraud, but that's not always going to be the case. A lender's solicitor has duties to ascertain the ID of the Borrower and/or may also be party to the lender's due diligence about the Borrower, and/or have contact with the mortgage intermediary which might put him in a better position to identify an imposter than the imposter's own solicitor.
- **Well trained staff, good systems and good processes are essential.** No system is fool proof, but this could prevent you being unwittingly caught by a fraud and/or if you do get caught out, could give you the upper hand in pursuing or defending a contribution claim. There is plenty of excellent guidance out there on ID, AML and Risk Assessment good practice and procedure.
- **Make full use of the safeguards which already exist.** When acting on purchases and re-mortgages, always advise your client to register with the Land Register Property Alert Service and to update their contact details with the service as required (if a property is to be let out, the alert should be set to the home address of the client, not the property address). This might just be enough to stop the next fraud.

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Re-mortgage: Lender repossesses and sells on

Case study #4: A further twist (no breach of trust?)

Another imposter Borrower situation, but this time the true owner doesn't discover the re-mortgage fraud until after the bridging lender has already repossessed the property and an innocent third-party purchaser is in possession.

The true owner seeks an indemnity from HMLR for the entire loss of his property. HMLR pays the indemnity and then looks to recover its losses.

Standing in the shoes of the true owner, what is HMLR's cause of action? The re-mortgage proceeds were certainly held on trust for the lender, but the lender has recovered its advance on the repossession sale and has suffered no loss.

By contrast, neither solicitor acted for the true owner, so how can they have held any monies on trust for him? In this scenario, there's no breach of contract claim let alone a "slam dunk" claim for breach of trust. HMLR may have to establish that a duty of care was owed, and that the duty was breached.

So, it's back to issues of good training and good systems and procedures.

Practical take-aways

- **Be alert to fraud in all property related transactions.** Fraudsters are sophisticated and continually find new methods and new targets. While previously a fraudster might have acquired a false passport, now he might obtain a re-issued driving licence enabling valid utility and bank accounts to be set up enabling a much more sophisticated identify fraud, including changes of name by deed-poll. The targets for fraud are also changing: while we might typically have seen frauds on high value property sales, we are now seeing them on both lower value transactions, and also in re-mortgage and bridging finance cases.

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Identifying and addressing red flag issues

If you're acting for a Buyer, is it a good idea to ask the Seller's solicitor whether they've taken steps to verify their client's identity, and a connection with the property? What happens if you ask but then fail to follow up, or if the Seller refuses to answer?

If you are acting for a Seller and the Buyer's solicitor asks you to confirm that you are satisfied with evidence of identity or of an association with the property being sold? Should you answer?

In Dreamvar itself, the court accepted that, "*absent any indications to the contrary*", it was not negligent for Solicitors for Buyers to assume that the Seller's solicitor has competently and reasonably carried out the necessary identity and other checks. Dreamvar also suggested that Sellers' solicitors can in certain situations be said to have given a warranty that they are authorised to act on behalf of the true registered proprietor.

This would suggest that a reasonable default position for practitioners is for Buyer's solicitors to assume competence on the part of the Seller's solicitor, and for Seller's solicitor to decline to answer this type of enquiry. Moreover, if completion monies are paid away by Sellers' solicitors to a fraudster, and the Code applies, then according to Dreamvar the Sellers' solicitor will be in breach of undertaking and will ultimately have to pick up the Buyer's claim irrespective of any questions raised, and any answers given.

However, this only applies if there are no indications to the contrary. So the guiding principle in all transactions must still be to look out for those "indications" that all is not well and then to consider what is in the best interests of your client. This could make the difference between a serious fraud happening or not happening and if the fraud still goes ahead, could be significant on a contribution claim.

Case study #5: Should have followed up on those "*indications to the contrary*"

Both sets of Solicitors have copies of the Borrower's ID documents in respect of a re-mortgage transaction, but sadly (perhaps because they are more interested in having the documents rather than looking at them) neither notices that the spelling of the Borrower's surname on his utility bill does not match his passport. As the transaction proceeds, solicitors for the lender became aware that the lender has spotted the spelling discrepancy. Not only that, they are also told by the lender that an AML search has come back 'referred': the Borrower was on the electoral roll for the security address even though he is purportedly living elsewhere; and the Borrower's bank statements do not evidence receipt of salary and are not consistent with his working in London.

These are classic "indications" requiring questions to be asked, but in this case solicitors for the lender neither raised the possibility of fraud with their own client, nor raised concerns and questions of the Borrower's solicitors who remained blissfully unaware of the multiple additional issues known about by the other side.

In this scenario, in a contribution claim as between the two solicitors it has been successfully argued that the lender's solicitors should bear the lion's share of responsibility for the lender's loss.

Practical take-aways

- **Ensure that you verify identity to the Safe Harbour scheme standard insofar as possible.**

Conveyancers should all know by now that HMLR has set out a digital identity standard involving biometric and cryptographic checking of identity and verification that an individual really is who he says he is.

HMLR confirms that the standard is regarded as a discharge of the duty to verify the identity of a party to a registrable transaction, and that a conveyancer who adopts this approach will have reached a Safe Harbour i.e., will have fulfilled his obligation to take reasonable steps in relation to the requirement to verify his client's identity.

A "Safe Harbour" standard will not be achieved where there is reasonable doubt as to the checks or the bona fides of the parties, and that doubt is not positively resolved. Where it's not practicable to carry out enhanced checks or to resolve doubts, conveyancers will remain at risk of HMLR seeking recourse.

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The guidance states that where a conveyancer carries out the steps required in the Safe Harbour standard: "HMLR will not pursue any recourse claim against the conveyancer resulting from the registration of a fraudulent transaction on the grounds that their identity checks were inadequate".

A strict interpretation of these words might mean that HMLR can still pursue breach of trust claims. We'll have to see. But if the technology is all it's cracked up to be, it surely must mean that if you achieve the standard, the chances of acting for an imposter (and hence the risk of being in breach of trust) must be dramatically reduced.

It's almost certainly the case that had the technology underpinning the Safe Harbour scheme been in place at the time of the Dreamvar transactions, both involving false passports, those frauds would have failed at the first hurdle.

- **Do not rely purely on identity checks as your fraud risk control - ask additional questions where necessary.**

While meeting the Land Registry digital ID standard requirements should significantly reduce the incidence of fraud, it is essential to be alert to all potential risk factors - and the greater the incidence of risk factors, the more important it is to obtain definitive documentation that only the real owner of a property could have. Utility bills, council tax, home insurance documents, rental packs, etc. can be valid, yet not do anything to 'prove' ownership.

Even where you reach the Safe Harbour, the scheme refers only to the client's identity. What if the client can get through the identity check (e.g. the client has changed his name by deed poll to the name of the registered proprietor and now has a driving licence and bank account to match)? There is still a vital role-especially for those acting for sellers, for intelligently assessing risk in the round: fraudsters are nimble and inventive so continuing to look out for the well-known red flags and to seek genuine connections between the client and the property to be sold or re-mortgaged will always stand you in good stead.

- **Look for a wider range of warning signs that might flag a fraud. The following are examples of questions from real cases which, had they been asked, might just have been enough to scare off a fraudster, or at least alerted the firms in question to the fraud risk:**

- > Can the client really have owned the property that long - he looks so young?
- > Why have all the ID documents only been issued within the last few months?
- > Why is the client on the electoral roll for a property he rents out?
- > Why isn't there a regular monthly income that matches the rental agreement I'm being shown?
- > How can the client have afforded to buy the property on that modest salary?
- > Why hasn't the client retained any planning documents from when he replaced the windows?
- > Didn't the client keep any documents from when the property was bought?
- > Who acted for the client on that purchase?
- > Why is the sum insured on the schedule the equivalent of the value of the property rather than just the re-instatement value?
- > Why are groceries being purchased in Manchester when the client lives in London?
- > Is the name on the utility bill spelled correctly? Isn't the bill a bit high for an empty property?
- > The property only has two bedrooms, why does the SPIF give information about three?
- > Why does the EPC refer to a first floor flat, when the property is on the ground floor?
- > If the client really owns the property, why is he getting aggressive when I ask him these questions?

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Conclusions

Pre Dreamvar the risk fell almost exclusively on Buyers' solicitors. Now, it is solicitors for Sellers (and re-mortgage Borrowers) who carry most risk for imposter fraud. It is not commercially realistic to act only for Buyers, and anyway, the nightmare scenario whereby the Seller's solicitor is uninsured cannot be eliminated.

No one wants to be intrusive or to bombard a client with questions, but applying a healthy dose of scepticism to what you are being told and shown might just make all the difference. While clients may initially resent the due diligence requirements, most should be able to understand that these checks help protect them, and fundamentally, an honest client has nothing to lose in being open.

We'd all like the real villains, the imposter-fraudsters, to have to pay for their crimes. But they are rarely caught. The 2022 Economic Crime & Corporate Transparency Bill proposes a new offence of 'failing to prevent fraud', with stronger powers and higher fines likely to be available to regulators for firms that are not doing enough to identify fraudsters. Conveyancing solicitors can do their bit by not letting the fraudsters get past first base. As the way we work and the regulatory controls constantly evolve, so do the ways that fraudsters operate - so it is essential that you keep your fraud controls under regular review to ensure that they are fit for purpose.

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