

# When conveyances go wrong

A High Court case highlights the risks of not lodging a caveat on the property you're under contract to buy.

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**CAVEATS** are the traditional way in which someone with an equitable interest in a property can protect their interest in that property.

The High Court case of *Black v Garnock* in 2007 suggests that buyers under contract should always lodge a caveat and shows the risks of not doing so.

So in which circumstances should a caveat be asked for and lodged, and what are the key ways of removing unwanted caveats? Also, how can title insurance lay off risk in this area?

## THE HIGH COURT CASE

The case of *Black v Garnock* involved the following facts. A seller and buyer executed a contract for the sale of Torrens title land. The buyer didn't lodge a caveat against the title of the property after exchange of contract. Two hours before settlement, the Registrar-General recorded a writ of execution in favour of a judgment creditor of the seller against the land. (A judgment creditor is a party to which a debt is owed.)

The buyer was unaware of this. Their solicitor had carried out a title search earlier in the day and the search hadn't revealed anything untoward.

Settlement proceeded but the buyer was subsequently informed that the transfer couldn't be registered because of the writ of execution.

The buyer applied for an injunction and consequential relief prohibiting the execution of the writ by the sale of the land to a third party.

The High Court held that the buyer wasn't entitled to this injunction under section 112 of the *Civil Procedure Act 2005 (NSW)* and the provisions under the *Real Property Act* in relation to the recording of writs (and caveats).

While a detailed analysis of the sections in relation to writs is beyond the scope of this article, it's sufficient to note that while writs of execution don't create proprietary interest in land, they are capable of registration on the title and for the period of their effective life, confer rights upon the Sheriff to deal with the land by and on the face entirely of the Register.

Once a writ of execution is registered on the title of the property, it obtains priority over any other equitable interest that hasn't been noted on the title.

The significance of *Black v Garnock* is that it stresses the importance of buyers protecting their positions by lodging a caveat on the title. If the buyer in this case had lodged a caveat upon the title, their equitable interest in the property would have obtained priority over the interest of the judgment creditor. The buyer would have also been notified when the judgment creditor sought to register the writ of execution upon the title.

While it's prudent for buyers to lodge caveats against the title of the property, it doesn't appear to be a common practice. Unfortunately for the buyers in *Black v Garnock*, the failure to lodge a caveat against the title has proved to be very costly.

## THE REAL PROPERTY ACT AND CAVEATS

In order to have a caveat removed from the title of the property, the registered proprietor or the holder of the equitable interest in the land may apply to the Registrar General to serve a lapsing notice upon the caveator. (The caveator is the person who lodged the caveat.)

The effect of this lapsing notice is that unless the caveator takes steps to extend the operation of the caveat, then the caveat will lapse within 21 days of the date of service of the lapsing notice.

If a caveator wishes to extend the operation of the caveat after he/she is served with a lapsing notice, they must approach the Supreme Court.

The practical way in which this is achieved is that the caveator, generally with the help of a solicitor, prepares a summons and a supporting affidavit. These documents are then ideally served upon the registered proprietor before the caveator approaches the Supreme Court for the order extending the operation of the caveat.

It happens in practice that the applications to extend the operation of the caveats occur just before the caveat lapses and it's usually the case that the caveator, through their legal counsel, will have to approach the duty judge for the orders sought in the summons.

In order to be successful, the caveator has

to essentially demonstrate to the court that they have a legitimate equitable interest that's capable of being protected by caveat and also provide an undertaking that if they're later shown not to have a legitimate caveatable interest and have caused the owner loss and damage as a result of the lodgement of the caveat, then they will compensate the owner accordingly.

An application for extension of the caveat is usually brought before the duty judge on more than one occasion, as the duty judge invariably doesn't have the time to deal with it in its entirety the first time round. This can make an application to extend the operation of the caveat quite costly as it invariably involves more than four visits to the court.

In addition, anyone who has, or claims to have, an estate or interest in the land that is the subject of the caveat may apply to the Supreme Court for an order that the caveat be withdrawn by the caveator.

There are restrictions on the lodgement of further caveats by the same caveator if the early caveat lapses or is withdrawn. The *Real Property Act* also provides that compensation may be payable in certain cases.

## TITLE INSURANCE

Another way for buyers and lenders to protect themselves is to purchase title insurance.

### Residential lender title insurance

Title insurance is a product that was developed and sold in the United States. It's designed to protect lenders in the event that they're required to realise on their security and suffer loss as a result of certain defects covered by the insurance policy. Cover is generally for actual loss, not exceeding 125 per cent of the amount of indemnity covered by the policy.

Title insurance is taken out by lenders (but paid for by the buyer) to cover them for risk in the mortgage documentation, settlement and registration process including:

- identity and title fraud;
- gap cover for the period between advancing funds at settlement and registration of documents;
- where the mortgage isn't valid and enforceable as an encumbrance against the title;
- the mortgage doesn't have the correct priority;
- outstanding rates on the property resulting in a claim against the secured property;
- instances of duress, incompetence or incapacity;

- any defects that would have been revealed by an up to date survey including encroachment of improvements;
- non-compliance with covenants and restrictions on title;
- title to the land is unmarketable;
- any defect or lien or encumbrance on title which is unknown to the lender;
- invalidity or unenforceability or any assignment of the mortgage;
- any adverse circumstance which affects the land and that would have been disclosed by searches of public records;
- fraud which discharges, varies or affects the insured mortgage or causes a loss in its priority;
- improvements constructed after settlement which encroach upon or interfere with an easement or right of way;
- encroachment of an improvement onto the land secured by the mortgage constructed after settlement by someone other than the owner;
- lack of necessary approvals for existing structures on the property or modification or replacement of the existing structure after settlement.

Title insurance also provides cover for the costs of defending proceedings based on the covered risks.

Let's look at an example from insurers Stewart Title Limited of a real life claim in circumstances where the lender held title insurance.

A lender loaned money to a borrower to purchase a house. After receiving payments regularly the loan went into arrears. When enforcement proceedings began, the lender learned that a forced discharge of their mortgage had been registered some time earlier although mortgage payments had continued to be made. After the mortgage discharge was registered, the borrower sold the property to an innocent buyer. The lender's insured mortgage was unenforceable against the title. In this situation, the lender was paid out the balance owing on the mortgage by the insurer.

**Commercial lender title insurance**

Commercial lender title insurance is available against properties that are zoned commercial, industrial, retail and mixed use. Commercial lender title insurance is a contract of indemnity that provides cover for risks which are inherent in the lending transaction.

It covers similar risks to residential lender title insurance, as set out above. In addition, it also covers the risk arising in the period between advancing funds at settlement and registration of documents.

As with residential lender title insurance,

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defence costs are also covered under the policy. The costs of defending proceedings based on covered risks or in relation to defending the validity or priority of the insured mortgage are covered.

An example of a claim scenario could be where a lender takes an equitable charge over a property for a loan and is unaware at the time of the provision of the loan that the registered proprietor has already given an equitable charge over the property which hasn't been noted on the title of the property by way of caveat. In general, the interests of lender and holder of the equitable charge second in time would be postponed to the interests of the first lender. If the proceeds of the property are insufficient to discharge both loans, title insurance can come into play to compensate the second lender.

Another example is where a husband obtains a mortgage over the family property by fraud and the wife successfully has the mortgage set aside in relation to her share of the property. The lender would be entitled to indemnity under the policy.

**Purchaser's title insurance**

Purchaser's title insurance is now available in Australia and covers the purchaser from the *date of settlement* to the date of resale of the property for a one-off premium paid at the date of settlement.

It typically covers similar risks as residential lender title insurance except the insured is the buyer. Significantly however, it also covers mortgage or title fraud after settlement, incorrect signature of a document, defective registration of a document and problems with the registration gap (eg. issues arising in *Black v Garnock*).

The title insurer will also defend any challenge to the insured's title, and if ultimately unsuccessful, will indemnify the insured against their loss if an insured risk occurs.

**LEGISLATION AMENDMENTS**

In addition to title insurance, there is a Torrens Assurance Fund whereby victims of mortgage fraud are able to make a claim for their loss and damage.

Amendments to the *Real Property Act*

1900 and *Conveyancing Act 1919* which came into force on May 13, 2009 are targeted at ensuring that lenders take reasonable steps to confirm the identity of the mortgagor before presenting a mortgage for lodgement and registration at the Land Titles Office.

A failure to do this can now lead to the cancellation of the recording of the mortgage from the title of the property.

**CONCLUSION**

Caveats have been and continue to be the traditional way in which holders of equitable interest in real property can protect their interest in the land. Not only is the Registrar-General compelled under the *Real Property Act* to notify the caveator in the event of any dealing that's sought to be registered against the title, the Registrar-General is also prevented from registering any dealing so long as the caveat remains enforced.

Title insurance is important and can protect the interest of lenders and buyers. However, as buyer's title insurance only protects the owner from the date of closing, it still leaves the buyer open to the risk of competing legal or equitable interests that are created prior to the date of settlement. This is because it's still possible that the buyer's equitable interests may be postponed to another equitable interest created either before or after the date of exchange.

The most effective way to protect a buyer's interest from the date of exchange to the date of registration of the transfer on the title of the property is with the lodgment of a caveat as soon as contracts for sale have been exchanged. While the caveator may have to incur in the order of \$10,000 to \$20,000 if his/her entitlement to the caveat is challenged, this must be viewed as relative to the value of the property being purchased. A cheaper alternative is obtaining purchaser's title insurance which is significantly cheaper and will protect the interests of the buyer in the majority of cases.

It would certainly have protected the buyer in *Black v Garnock*. [api](#)

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