THE LAW SOCIETY OF TASMANIA

A PROFESSIONAL RESPONSIBILTY BEST PRACTICE GUIDE FOR LAWYERS:

TITLE INSURANCE

OBJECTIVE

This best practice guide has been prepared in response to law firm queries and concerns raised with the Society regarding title insurance, referral arrangements, and the practise of recommending financial (insurance) products to clients. It has been developed to assist legal practices to conscientiously navigate and carefully consider their involvement in the arrangement of title insurance on behalf of clients, as well as to consider its place in the provision of legal services.

This guide is not intended to constitute legal advice and the Society recommends practitioners exercise their experience and judgement in applying the guideline to their subject matter. This document is not all-encompassing and is not an exhaustive list of every issue that may arise for consideration in a referral context. Practitioners will need to adapt it to address individual client circumstances.

Hyperlink to end-of-document Summary / Conclusions **here**.

BACKGROUND

Involvement with financial instruments can be a part of everyday practice for commercial legal practitioners, whether it be to advise upon their legal terms (e.g. share acquisitions) or simply to recommend their purchase, where such a consideration by necessity arises in the context of providing legal advice (e.g. recommending home and contents insurance, where risk passes to the purchaser upon entry into a contract of sale).

Title insurance has more recently been added by many law firms to their suite of insurance recommendations made in association with property purchases.

It has become recognised as a product offering cover in relation to some risks that may cause a purchaser loss or otherwise affect their ownership, such as boundary defects or illegal building works not known by the purchaser at the completion of their purchase. It is seen by many practitioners as a useful and affordable supplementary risk management tool for clients where it offers protection against matters that might not be revealed by searches.

Recommending insurance has, however, traditionally taken place within legal practices adopting an arms-length approach. The insurance is recommended for legal reasons and clients are encouraged to shop around for a policy that suits them. Any 'arranging' that takes place as agent for the client at his or her instruction has also been done at arms-length.

A unique feature that has been introduced to Australian legal practices by new-to-market title insurance providers has given rise to calls for guidance. This feature is an insurance procurement model that takes law practices beyond general recommendations to the next level of introducing specific products to clients as well as offering to arrange their acquisition. These referral arrangements offer to the law practice a provider-paid fee-for-service return. They also offer protections against certain *Corporations Act* compliance concerns (e.g. an exemption from the need to hold an AFSL) as well as indemnities, waivers and excess layer PI insurance.

The introduction of such referral arrangements, with their own sets of terms and conditions between the law practice and the insurance provider, has however presented a number of complex considerations to navigate. Corporations law obligations, professional responsibilities and ethical duties owed to the client are all in the mix.

In late 2018 the Law Society of Tasmania was requested to issue written guidance to the profession. After considerable legal consultation and consideration, the Society has approved this best practice guide, which aims to set out the basic associated considerations for law firms under each of the *Corporations Act 2001* and the Common Law.

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INSURANCE, TITLE INSURANCE, THE REGULATORY FRAMEWORK, AND REFERRAL ARRANGEMENTS

The abovementioned types of insurance products are financial products under the corporations legislation. The recommendation and arrangement of financial products therefore typically requires careful consideration by law firms from a federal regulatory perspective. No less important are the professional responsibility and ethical considerations for lawyers.

1. RECOMMENDING INSURANCE – THE CORPORATIONS LAW FRAMEWORK – BACK TO BASICS

1.1 Firms who choose to recommend and/or arrange financial products on a regular basis need to be mindful of the *Corporations Act 2001* (the Act). This is because prima facie, their conduct might amount to a 'financial service' under the Act and they risk being found to be carrying on a 'financial services business' within the meaning of s.911A(1) without authorisation. Persons carrying on a financial services business are, as a general principle, required to hold an AFSL or be an authorised representative of the holder of an AFSL.

1.2 Practitioners recommending specific financial products or classes of financial products should therefore familiarise themselves with S766B (definition of financial product advice) as well as the exemptions that apply. Where arranging occurs on behalf of the client practitioners should also familiarise themselves with S766C (meaning of dealing in a financial product), as well as the exemptions that apply.

1.3 Section 766B of the Act reads [excerpt]:

*'For the purposes of this Chapter, **financial product advice** means a recommendation or a statement of opinion, or a report of either of these things, that:*
(a) is intended to influence a person or persons in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products; or
(b) could reasonably be regarded as being intended to have such an influence.

1.4 All relevant circumstances are to be taken into account in determining whether *financial product advice* is given (ASIC Regulatory Guide RG 36).

1.5 In one of the leading decisions in relation to what constitutes financial product advice, the NSW Supreme Court found that an implied recommendation or statement of opinion might occur for example where information is presented in a way that favours or commends a particular course of action or implies that the view of the presenter of the information is that the contemplated course of action is likely to be beneficial to the client (s*ee Australian Securities and Investments Commission (ASIC) v Park Trent Properties Group Pty Ltd (No 3)* [2015] NSWSC 1527 per Sackville AJA at [365] and [366]).

1.6 Whilst a recommendation that a client acquire certain insurances may be objectively determined to be a necessary aspect of a practitioner's legal advice and service package, it is the Society's view that the acts of referring to risks and possible exposures in a letter of legal advice followed by a reference to a *specific* financial product (e.g. 'Provider X's Y Insurance') and an offer to arrange the acquisition of that financial product, may amount to the provision of financial product advice by a practitioner. It is also the Society's view that the correspondence alone is likely to imply that the view of the practitioner is that the decision to purchase that insurance product is likely to be beneficial to the client. Given the solicitor-client relationship is one which is understood as entailing influence, the nature of the relationship is a critical consideration in determining whether the circumstances give rise to an act of influence.

1.7 The Society at the same time acknowledges the exclusions set out in section 766B(5) (legal advice exemption) of the Act and reg 7.1.35A of the *Corporations Regulations 2001* (dealing, agent on instruction from client).

1.8 Sub-section 766B(5) provides that the following advice is not financial product advice:

> (a) advice given by a lawyer in his or her professional capacity, about matters of law, legal interpretation or the application of the law to any facts;
>
> (b) except as may be prescribed by the regulations--any other advice given by a lawyer in the *ordinary course of activities* as a lawyer, that is *reasonably regarded as a necessary part* of those activities (emphasis added).[1]

1.9 Sub-section 766B(5) therefore creates a limited exception to the broader definition of financial product advice.

1.10 Practitioners must therefore carefully consider the nature of their activities as well as the content of the advice that is provided to clients. The insurance recommendation would need to be soundly linked into the advice.

[1]The *Corporations Regulations 2001* (the Regulations) do not include any prescription for the purposes of this exemption.

1.11 Template letter disclaimers that stipulate, after recommending the product, that 'this does not constitute legal advice' or 'we cannot provide advice in relation to this product' will *ensure* the exemption in ss766B(5) does not apply. The recommendation will then amount to 'financial product advice' within the definition of the Act. The disclaimer will not be legally effective because it is not possible for a practitioner to contract out of the provisions of the Act, nor to limit his or her liability in this way.

1.12 Section 766C of the Act and its associated regulations create a number of exemptions to the definition of dealing in a financial product, including where that dealing is as an agent or representative of another (see reg 7.1.35A of the Regulations).

1.13 Whether the total activities referred to in 1.6 above would fall within the legal advice exemption ss766B(5)(a) and (b) or reg 7.1.35A will also no doubt be assessed in all the circumstances. This question is something to which practitioners ought in every case direct their attention.

1.14 Also for consideration is that whilst *arranging* insurance on behalf of clients as agent may attract the s766C 'dealing' exemption under reg 7.1.35A, if the firm receives payments by an insurance product provider for the arranging service, this exemption will not apply.[2]

1.15 The exemptions referred to in paragraphs 1.7 – 1.14 are unlikely to be relevant to legal practices that have chosen to enter into a referral arrangement. Those practices will still, however, need to consider what additional obligations the common law, as well as the terms of the referral arrangement, might impose upon them (discussed further below).

2. REFERRAL ARRANGEMENTS

2.1 Title insurance referral arrangements appear to have over the last 10 years proliferated throughout the legal services industry Australia-wide.

2.2 In so far as direct recommendations and remunerated procurements are concerned, issues relating to the possible contravention of s911A(1) of the Act have been dealt with through the introduction of authorised distributor arrangements (where the insurer holds an AFSL) or representative arrangements where the insurer has the benefit of an AFSL exemption. Where an insurer holds an exemption under s911A(2)(g) of the Act, practitioners who become participants of their referral arrangement become representatives who are also exempt. That exemption is engaged where the insurer is a body regulated by the Australian Prudential Regulation Authority (APRA), the service is one in relation to which APRA has regulatory or supervisory responsibilities and the service is provided to wholesale clients. Currently, title insurance is not a form of insurance that is regulated as a product provided to retail clients.[3]

3. ENTERING INTO ARRANGEMENTS WITH INSURANCE PROVIDERS - THE LIMITATIONS OF WHAT PRACTITIONERS CAN AND CANNOT ADVISE ON

3.1 Practitioners need to exercise care when considering the terms and conditions of proposed referral arrangements in the context of a solicitor-client relationship. If a practitioner acts outside the terms and scope of the referral arrangement, 'financial product advice' may be

[2] Sub regulation 7.1.35A(d), *Corporations Regulations 2001*
[3] Section 911A(2) of the Act, when read with *Corporations Regulations 2001* regulation 7.6.01 and s.761G of the Act.

provided or 'dealing in a financial product' may be occurring, where he or she is not authorised to do so.

3.2 Practitioners acting as representatives also need to be satisfied that the terms and conditions of the referral arrangement do not give rise to conflicts between duties owed to the client and the practitioner's obligations under the referral agreement with the insurer (see further under section 8 below).

PROFESSIONAL AND ETHICAL CONSIDERATIONS

4. RETAINER AND PROFESSIONAL RESPONSIBILITIES

4.1 If a referral arrangement has been entered into by a practitioner, they may have addressed their *Corporations Act* and AFSL obligations.

4.2 Are additional *legal professional responsibilities* triggered? Critical for consideration, is that where a practitioner makes a recommendation or gives advice about a specific financial product (whether that advice has been requested or not) it will doubtless broaden the terms of the retainer beyond the giving of legal advice. Duties are also broadened. Accepting that the content of the duty of care is a fact specific inquiry, it will likely embrace a number of duties broadly equivalent to those of an insurance agent and broker including:

(i) a duty to give accurate advice about the meaning and content of the policy document; including advice as to when indemnity is available and in what circumstances the exclusion clauses will operate;

(ii) advising the client of the risks they might face which might be lessened by indemnity insurance;

(iii) advising the client about the suitability of the policy, for the particular circumstances of the client; and

(iv) ensuring the information contained in the policy proposal form is accurate and complete.

4.3 Practitioners should exercise caution in using information provided by the insurance provider either to be incorporated into a solicitor's letter or to be included as an enclosure with that letter. This is because it may trigger a broadening of the retainer with additional duties to the client.

4.4 Because a specific product is being recommended, practitioners should also be mindful of their duty to avoid any compromise to their professional independence as well as their duty to act in the best interests of the client. Care should be taken to advise the client there may be products better suited to their needs on the market and they may wish to 'shop around' (see further 8.3 below).

5. FEES PAID BY INSURERS TO LAWYERS IN CONNECTION WITH ARRANGING TITLE INSURANCE

5.1 Practitioners must not:

(i) obtain a personal benefit at the expense of the client;

(ii) make an unauthorised profit, absent full disclosure and informed consent; or

(iii) accept a secret commission; and

(iv) must at all times act in the best interests of the client.

5.2 Whilst a fair remuneration for service (with full disclosure to the client) may be acceptable per se under solicitor professional conduct rules, the terms of the payment under the referral arrangement must be examined carefully to ensure no conflict arises. For example, the provision of an election to either take a fee as a processing fee or to give it to the client (by way of premium reduction or otherwise) at once gives rise to a choice that may confer a personal benefit upon the practitioner at the expense of the client. Accordingly, this type of offer by an insurer gives rise to a conflict of interest for the practitioner. Likewise, a requirement to keep all or part of the financial arrangement *confidential* (including the potential loss of a 'service fee' where a purchased policy is withdrawn by a client during a cooling off period) is unacceptable as it raises the spectre of a secret commission, that a fiduciary is not entitled to receive.

6. THE USE OF TITLE INSURANCE AS AN ALTERNATIVE TO USUAL CONVEYANCING SEARCHES / PRACTICES

6.1 Regardless of whether a referral arrangement exists, the Society does not support the use of any title insurance product as a substitute for the exercise of reasonable skill, care and competence in acting for a purchaser client in a conveyancing transaction. This includes undertaking the usual searches and giving advice to the client about the results. These obligations must not be compromised by the use of title insurance where the practitioner has been engaged to provide legal services to the client.

6.2 Insurance should be used as a tool to augment legal services, not devalue or replace them. Where dispensing with certain searches (e.g. a s337 *Local Government Act 1993* search) is raised as an option (by the practitioner or the client), the client would need to be fully informed regarding all associated risks and the client's express agreement would need to be obtained.

For example, the failure to identify certain matters during the conveyancing process by not undertaking the appropriate searches may mean the client suffers a lost opportunity to rescind the contract or to obtain other remedies from the vendor. He or she may also be left inadequately covered by the policy of insurance, or not at all. Providing this option would again trigger additional responsibilities and the practitioner's advice would need to extend to advice on the policy wording (and level of cover) itself. In other words, a release from the obligation to undertake such searches must be a fully informed release.

7. INSURANCE PROVIDER, WAIVER AND INDEMNITY

7.1 Referral arrangement offerings by insurers to prospective legal practices may include certain indemnities, waivers, and 'excess layer' PI insurance provisionings. Again, the wording of the relevant terms and conditions should be examined closely.

7.2 It is also important that practitioners check the limits of the excess insurance layer as well as any indemnity. For example the indemnity may be limited to only those circumstances in which the title insurance policy itself would have responded, had a claim been made under that policy. If the claim or part of the claim against the practitioner is that the client has lost an opportunity to rescind the contract of sale (which they would have been in a position to do had a particular search been conducted and the relevant circumstances revealed) the indemnity may not apply.

8. CONFLICTS OF INTEREST AND OTHER FIDUCIARY DUTY CONSIDERATIONS

8.1 Acting for a client while also acting as a representative for an insurance provider obviously raises a question of conflict of interest and duty. The obligations set out in terms and conditions of the referral arrangements may intersect inconsistently with the duties that a practitioner owes to a client, and practitioners need to carefully consider the fine print.

8.2 The referral arrangement terms and conditions may result in a conflict in relation to disclosure. For example, where the practitioner is instructed by the client to withhold relevant information from the insurer (e.g. where searches conducted reveal information relevant to policy coverage) this might constitute a breach of the terms of the referral agreement, put the indemnity/waiver coverage at risk, and attract other liability. This is a clear conflict of interest and duty issue.

8.3 A fiduciary relationship of course creates many legal duties for the person in whom the trust has been placed. Perhaps the most significant matter of concern in 'referral and arranging relationships' arises from a practitioner's duty *to avoid any compromise to their professional independence*, and, again, their duty to always *act in the best interests of the client*.

If a practitioner / firm chooses to enter into a referral arrangement, they are recommending a specific product. As noted above, the additional duties triggered may require them to explain that specific product before arranging it on the client's behalf. Title insurance *itself* may, in the practitioner's opinion, certainly be in the best interests of the client. In the circumstances specific to that client. But is *the specific product being recommended* in their best interests?

By virtue of the fact there are other products on the market, the specific product they are recommending might not be best suited to the client. If a practitioner were to advise on the terms of a product they have recommended (as required by their new additional duties), they would no doubt then have the responsibility to advise the client of other products on the market *and* explain the terms of those products as well. Or at the minimum, explain there may be more suitable products and offer to provide advice in relation to those products also.

A client who has taken up the practitioner's offer 'in the moment that is presented to them', might subsequently return with a claim (or complaint) that another policy had better premiums, or that due to different exclusion clauses another policy would have responded to their subsequent predicament. They may point to the element of influence that was present at the time they were steered towards the first product.

9. SUMMARY

9.1 Practitioners who as part of a conveyancing transaction see benefit in title insurance may provide generic factual information and advise clients generally as to the insurance's availability when advising on insurance that ought be considered. Information that provides the names of known insurance providers who offer insurance relevant to their client's needs is acceptable if the practitioner's involvement with the insurer is at arm's length. Otherwise additional duties to the client may be triggered.

9.2 Whilst firms recommending and arranging insurance may benefit from financial services exclusions such as those found within ss766B(5) of the *Corporations Act 2001* or reg 7.1.35A of the *Corporations Regulations 2001*, or authorised distributorships or licence holding exemptions offered under referral arrangements, the content of the advice provided and the circumstances in which insurance is arranged must be carefully considered in the context of the same.

9.3 Practitioners recommending specific products must ensure that adequate advice is provided to the client. Disclaimers in letters of advice, or other attempts to limit liability, are not likely to be effective, even where there is a referral arrangement.

9.4 Recommending, arranging or advising a client to take out title insurance in substitution for legal advice and searches (*whether or not* an insurance referral arrangement exists) may not satisfy the practitioners' legal and professional obligations to their client. An informed consent and release would be required.

9.5 Referral agreements / arrangements between insurance providers and practitioners can create complex and potentially conflicting duties. How title insurance is obtained needs to be managed carefully.

9.6 Overall, practitioners need to carefully consider any activity that involves *putting forward* a specific financial product and offering to arrange its acquisition. They need to consider how they can act in the client's best interests without (1) providing advice on other available options (whilst still remaining compliant with the Act where not under referral arrangements with all providers) or (2) keeping well clear of financial product advice by advising them to 'shop around' for a policy acceptable to them (as is done with house and contents insurance).

This guideline does not constitute legal advice or an opinion on the merits of title insurance policies.