Once a fire is thought by the fire officer to have been begun deliberately, then the police are called in to pursue an investigation and, hopefully, to catch the person responsible.

It is the Bureau's hope that fire brigades will be able more effectively to help the police by preserving any evidence that exists on the fire scene and we have been assured that the majority of fire brigades do provide training to that end. We will encourage them to do the best they can in this respect. The Home Office will shortly be issuing a "Circular" to all Chief Fire Officers and Chief Constables reminding them of the importance of fire investigation and drawing to their attention examples of good practice.

Another important issue is the way in which the knowledge held by loss adjusters can be utilized. Loss adjusters tend to complain that they are kept at arm's length by fire officers and police. On the other hand it has been suggested to me that few loss adjusters are particularly knowledgeable about fire investigation. There is the additional problem that fire officers and police do not always differentiate between adjusters and assessors.

The Bureau is setting up a meeting at the Home Office with a view to improving the liaison between loss adjusters and the official agencies. In the case of fraudulent arson the adjustors may well possess information of significant value to the police. In turn it would be helpful if the police were able to communicate information they may have to the insurer - something which is not at present the case.

To cope with the educational issue we are talking to C.I.L.A. about setting up some instruction for loss adjusters in the techniques of fire investigation.

I am hopeful that as a result of the various efforts now in train - particularly the tougher stance which insurers are now having to take - the incidence of fraudulent arson will be contained.

2. MORTGAGE FRAUD
by Robert Goldspink, Denton Hall Burgin and Warren

Introduction

Mortgage fraud has been attracting an increasing amount of media attention over the last 12 months. Research carried out by one consultancy group suggested that one in 20 mortgages is fraudulent. This figure has been rejected as a considerable overstate-

ment by, amongst others, the Council of Mortgage Lenders and the true level of mortgage fraud in England and Wales is unknown and likely to remain so.

A study undertaken last year by Liverpool University indicated that Police forces were investigating more than 1,000 cases of mortgage fraud involving a sum of £500m. Recent reports indicate that the Metropolitan police have estimated the present value of mortgage fraud at more than £1 billion.

It is difficult to know whether the incidence of mortgage fraud did in fact increase in the late '80's or whether it is simply that an increasing number of mortgage frauds are coming to light because of the slump in the property prices. In the mid-1980's when property prices were booming, frauds involving over-stated valuations and inflated purchase price were more easy to conceal because Building Society repossessions, on average, did not take place until some 12 months after the mortgagee fell into arrears, by which time a considerable increase in the purchase price of the property was likely to have taken place which would at least help to mitigate the extent of the loss.

While the true scale and total cost of mortgage fraud will probably never be known, it is clearly a serious problem affecting not only the financial institutions which lend and their insurers who underwrite their Domestic Mortgage Indemnity ("DMI"), Crime and Employee Fidelity Policies but also for those insurers involved in the professional indemnity market.

In this paper I hope:

1. to provide information about the extent of the problem and practical example of its operation;
2. to highlight claims that are likely to arise in the event of mortgage fraud and therefore its relevance to insurers and their professional advisers; and
3. to give some practical advice on the ways in which mortgage fraud can be detected and its incidence diminished.

Section 1 - Extent and Example of Mortgage Fraud

Since, as I have indicated above, no firm figures on the extent of mortgage fraud are currently available I have decided to eschew "lies, damn lies and statistics" and will give you instead some practical examples of some mortgage frauds which have happened to have hit the newspapers.

In July this year an Edinburgh Court heard how one Defendant was involved in six

fraudulent mortgage applications between June 1989 and February 1990. The charges related to mortgage applications for a total sum in the order of half a million pounds, and despite the fact that a number of lending institutions refused his application when they became suspicious about the false details, the matter only came to light when the Defendant's brother complained to the police that his name was being used, falsely, on property deals. The theme of lending institutions pooling information and reporting suspicious applications to the police is one to which I will return later.

Another more gruesome case of borrowed "identities" was reported in February of this year when an estate agent was jailed for four years having admitted obtaining false names by searching cemeteries for children's grave-stones and obtaining birth certificates around which he set up identities for the purpose of making mortgage applications.

In a case at the Oxford Crown Court seven members of one family were charged with 75 offences including a £1.5m fraud involving 54 dishonest mortgage applications over eight years. The frauds were perpetrated with the help of false references, fictitious landlords and non-existent jobs.

One final and particularly memorable example is the case last year of the teenager sentenced to four years detention for fraud including obtaining a mortgage for £466,000 by persuading dozens of people that he was the youngest stockbroker in London and earning in excess of £200,000 per year.

My own practical experience of mortgage fraud has led me to distinguish between the borrower-led, one-off frauds and those frauds which generally result in more significant losses which involved the use of professionals such as valuers/solicitors and, possibly, the lending institution's own staff. With the help of a valuer to substantiate falsely inflated prices, the loss to the bank or building society is of course greater because in most cases they will have lent considerably more than the true value of the property over which they have their charge.

Section 2 - The effect of mortgage fraud on insurers

Policies which become relevant in the event of mortgage fraud have been tested to an unprecedented degree by the high incidence of claims arising from mortgage fraud and I anticipate that fundamental changes in the cover offered under these policies and the financial limits of that cover are likely to continue to be the subject of close scrutiny by underwriters if they have not been so already.

(a) Domestic Mortgage Indemnity Insurance

These policies which are also known as Mortgage Protection Policies were written in large numbers during the property boom to indemnify building societies against losses on mortgage advances. The policies I have come across were underwritten on a "master policy" basis where the borrower merely paid a "one off" premium without having any direct relationship with the insurer. Until relatively recently it seemed that building societies and insurance companies had enjoyed a very profitable relationship in the DMI business, but the unprecedented losses suffered by insurers under these policies in the last few years and predictions of even higher losses to come, have seriously threatened the future of this relationship.

Last month it was reported that Sun Alliance has refused to accept further DMI business from the Woolwich Building Society in a bid to contain the flood of claims. It was apparently estimated until recently that domestic mortgage insurance losses would be in the order of £2 billion with the problem reaching its peak last year and gradually tailing off as the economic recovery began. It seems likely, however, that with the recession showing no sign of abating, this estimate could well be exceeded.

The director of a specialist mortgage indemnity insurance broker was quoted in The Times this weekend as saying "30% of the market will be without cover by the end of the year". It seems that increasingly insurers are adopting a tough stance on the question of mortgage indemnity cover; several smaller lenders have been left without the means to serve first time buyers at all, and, at the same time, new agreements reached between the four main DMI companies, Sun Alliance, Royal Insurance, Legal & General and Eagle Star will leave lenders with lower levels of cover. Historically DMI cover related to the top 25% of the mortgage. Under the new policy wording cover will be further limited to 80% of the top 25% of the mortgage which effectively means that lenders will now have to carry the extra 20% risk themselves.

(b) Crime and Employee Fidelity Policies

The lending institutions' own insurance policies include Crime and Employee Fidelity Policies.

Building Society Crime Policies provide the financial institution with an indemnity in respect of direct financial loss arising from fraud by any person in connection with a mortgage or investment account. Such policies generally exclude "loss due to neglect, error or omission" and therefore the extent to which the employees of the insured in respect of these policies complied with their own checking procedures and the Society itself employed a sensible inspection system, must be of great interest to

the insurers who underwrite these policies.

Similar considerations apply in the area of Fidelity Insurance. Such policies are intended to protect an insured against loss incurred by reason or the breach of fidelity on the part of an employee. There are various ways in which an employee of a building society can become involved in mortgage fraud ranging from active involvement and participation in a systematic mortgage fraud ring to more low key bribery by way of generous hospitality and gifts from suspect mortgage brokers or surveyors with whom managers have become too friendly.

Statistics on the scale of employee involvement in mortgage fraud are very difficult to find. A recent study undertaken by the fraud department of KPMG Peat Marwick found that most large-scale fraud on companies is internal and that management is responsible for exacting three times as much money as other employees. The KPMG study also highlighted the fact that companies were most vulnerable in periods where management controls appeared to be more lax and this does accord with my own experience of institutional fraud. During the property boom of the 1980's most leading institutions concentrated on competing vigorously for business and making mortgage offers sometimes as quickly as 24 hours after the initial application rather than losing the business. It is unsurprising that in this climate checking systems fall down and corners are cut particularly in cases where employees are actively encouraged to engage in volume lending and receive bonus "incentive" payments linked to a number of mortgages that they "sell".

It is reported that certain officials in a number of banks and building societies are involved in a huge mortgage fraud ring to which I will refer again later (the Lucas case). Apparently the investigation by Scotland Yard's Fraud Squad has been handicapped by the complexity of the transactions involved in this £100m fraud and the need to rely on co-operation from lenders who are reported to be considerably "embarrassed" by the involvement of their corrupt officials.

Once again, I would suggest that underwriters of Employee Fidelity Policies might be well served to ask specific questions about their insured's internal checking facilities and the systems employed by the managers who oversee their insured's internal "systems security".

(c) Professional Indemnity Insurance

I do not think that I can justifiably be accused of undue sensitivity if I comment on the number of reported cases of solicitors' involvement in mortgage fraud over the last few months.

In many of these cases the fraud rings also involved the services of a valuer, although, not surprisingly, the word "solicitor" appears more often in the headlines.

In one recently reported case four solicitors were jailed for their part in a multi-million pound mortgage fraud involving a group of 19 people making 128 applications for more than 90 properties in the Greater Manchester and Lancashire areas. The Judge described the group as a "highly organised dishonest network" and highlighted the fact that with the right combination of dishonest people mortgage fraud was all too easy to commit. The professional property valuer involved gave falsely inflated values and the use of "borrowed" or fictitious names by the borrowers was reportedly backed by the solicitors involved.

The operation of professional indemnity insurance cover is somewhat different as between solicitors and surveyors and I will therefore consider these professions in turn. I also consider a clear distinction must be drawn between the operation of cover where a sole practitioner has been actively involved in a fraud as contrasted with a situation where the guilty professional has innocent partners who are jointly and severally liable for their partner's tortious acts. This is a distinction to which most insurers will be very much alive but it is often of strategic importance to third party claimants who are, or should be, aware that an insured may not recover any kind of benefit of indemity in respect of losses caused by his own deliberate crime.

Solicitors

Since the introduction of the Solicitors' Indemnity Fund in 1974, solicitors obtain the first layer of their professional indemnity cover not in the insurance market but rely, instead, on the "self insurance" fund administered by the Solicitors' Indemnity Fund, a company established by the Law Society. They go to the market for the top-up insurance.

The professional indemnity arrangements for solicitors are, however, relevant to third party claimants such as Building Societies and, of course, to their insurers in relation to subrogated claims, for example, where insurers have indemnified their insured Building Society under a Crime Policy and are seeking to recover their outlay from the party responsible for the loss.

The Solicitors' Indemnity Fund indemnifies solicitors in respect of claims for negligence and breach of contractual duty. Cover is given for loss arising from fraud or dishonesty of an employee and also fellow partners provided the claimant is not a party to the fraud or dishonesty. The S.I.F. will not, however, provide cover in the

event of the fraud of a sole practitioner or a partnership where all the partners are involved in the fraud.

The other fund upon which a claim can be made in the event of mortgage fraud is the Solicitors' Compensation Fund, established in 1942 with the basic aim of replacing "clients' money" misappropriated by a solicitor or employee.

In recent years there has been a substantial increase in claims in the fund. In the five years to 1991 the Law Society made payments totalling £6.8m to institutions mostly in relation to mortgage fraud. Last year the Compensation Fund paid out a total of £11.7m. The claims on the fund in respect of mortgage frauds seem set to continue and reputedly the largest mortgage fraud so far uncovered involving the well known case of Guy Lucas of R. Lucas & Sons, solicitors, is still under investigation by Scotland Yard's Fraud Squad.

Mr Lucas was as a sole practitioner allegedly operating at the heart of the fraud which ran for several years during the property boom of the '80's and which involved multiple mortgages backed up by false valuations on 200 to 300 mostly commercial properties. The estimated cost to banks and building societies involved was in the order of £100m and as a consequence of the "Lucas legacy" the Law Society has had to provide a minimum of £16m to cover possible claims from lenders who financed the purchase of the mostly commercial properties. This massive fraud is reported to be the major factor behind the announcement in June that most solicitors in England and Wales must pay an additional levy to top up the Law Society's Fund by £30m.

Those advising the victims of mortgage fraud should not, however, assume that the fact that, for example, a sole practitioner has been fraudulent rather than negligent gives an automatic entrée into the Solicitors' Compensation Fund. The Compensation Fund exists only to make payments of last resort, and the fact that a sole practitioner will not have the backing of the Solicitors' Indemnity Fund, does not obviate the need for victims of mortgage fraud to first exhaust their civil remedies against the fraudulent solicitor.

Negligence claims against solicitors unwittingly caught up in mortgage fraud are likely to be attractive to the lender who has been defrauded if they can find evidence that the solicitors involved failed to discharge their duty of care. I think it is likely that mortgage lenders will try to expand their standard instructions in order to try to assist them in proving negligence on the professional's part. If I were asked to advise mortgage lenders on their standard form wording, I would certainly ensure that the Solicitors' Report on Title highlight the solicitor's existing duty to disclose all

relevant facts about the transaction including details of any incentives, discounts or allowances which the purchaser is to receive. I was recently involved in a case where "cash back" bonuses were being paid to the purchasers which represented over 35% of the purchase price but which were not disclosed to the financial institution involved.

The Law Society's Legal Practice Directorate last year published certain guidelines for their members regarding the steps that could be taken to minimise the risk of fraud and what signs were to be watched for. Lending Institutions may well wish to highlight these guidelines in their instructions.

Surveyors

Notwithstanding the fact that prosecutions of surveyors and valuers do not appear to hit the headlines as often as those of solicitors, many lending institutions are concerned enough about fraudulent mortgage valuations to implement much stricter regimes in relation to those valuers who are permitted to act on their behalf in the preparation of valuations for mortgage purposes.

Unlike solicitors, surveyors obtain all of their professional indemnity cover in the market. All RICS members are required to carry professional indemnity cover to a minimum level of £100,000 in respect of practices with gross fees of £50,000 or less. Practices with gross fees in excess of this amount must carry £250,000 of cover. This limit is in respect of any one claim.

The fact that sole practitioners will have no cover for their own fraud has caused many lending institutions to remove sole practitioners from their panels. Some of you may have followed the correspondence instituted by RICS members in their professional journals and, in particular, in the Estates Gazette prompted by the effect such removal had on sole practitioners. The Secretary-General of RICS, in one letter, reminded the Council of Mortgage Lenderss that it is open to the Office of Fair Trading to consider whether to intervene in the matter and he made a reference to the issue being discussed during the informal sessions with the OFT. It seems likely that if RICS is to restore the confidence of lenders in sole practitioners it will have to instigate some kind of compensation fund possibly along the lines of the Solicitors' Compensation Fund.

Section 3 - How the effect of mortgage fraud can be minimised.

When (if?) the property market recovers the increased competition amongst lenders is likely, once again, to provide new opportunities for fraudsters. It is impossible to

suggest solutions which will result in the elimination of mortgage fraud but the application of a number of basic safeguards would help to minimise the effect of mortgage fraud. Those insuring lending institutions or professionals who are vulnerable to claims for breach of contract or professional duty may consider whether pertinent questions regarding the application of these basic principles should be included in the proposal/renewal form as a pre-requisite to providing cover.

Lending policy

Lenders should establish a clear and consistent lending policy outlining to all senior management the business standard required and ensure that all junior employees are alive to the possibility of mortgage fraud and the usual tell-tale signs to which I shall return shortly. In one case in which I was recently involved, the key to a substantial mortgage fraud ring was identified by a relatively junior branch employee who happened to attend an informal lunchtime discussion regarding mortgage fraud and noted the high incidence of early arrears amongst mortgages packaged by a certain broker. Further investigation revealed that the broker was indeed responsible for the presentation of mortgages on behalf a fictitious buyer with the assistance of a "bent" valuer.

Mortgage Broker

This brings me to the subject of brokers generally and in particular mortgage brokers who are involved in the practice of "packaging" mortgages. Lenders should be alive to the fact that mortgage brokers appear to have been at the centre of a number of fraud rings. The difficulty with pursuing a recovery action against such mortgage brokers is the fact that there is generally no privity of contract between the lending institutions and the broker and the difficulties in pursuing a tortious claim in respect of pure economic loss in the absence of any specific misstatement are well known.

In the cases in which I have been involved, a number of the fraud rings could be traced back to the brokers who were introducing "packaged" business to the society. Packaged mortgages are where the broker puts together and presents to the lending institution the signed mortgage application, the valuation and the necessary references and proof of income in line with the lending institution's general lending criteria. This practice saves both the lending institution and the borrower considerable time and was particularly utilised during the property boom when houses were changing hands extremely quickly.

The opportunity for abuse is obvious. The lending institution never saw the applicant face-to-face and had no control over the manner in which the income proof and

references were obtained. I would recommend that any lending institutions accepting packaged applications from now on should ensure that they have a written contract with each mortgage broker submitting packaged applications in this way. They should specify that the brokers involved must be covered by a professional indemnity policy and that, in respect of each packaged mortgage, a certificate should be provided by the broker confirming that the applicant is known to them that the references and personal details have been checked in accordance with specific guidelines to which I will return shortly. Needless to say, all valuations should be addressed to the lending institution.

Professional Advisers

The lender should select its professional representatives, including valuers, solicitors, brokers and agents introducing mortgages, with great care and preliminary checks should be made to confirm their professional status, independence and insurance arrangements.

Some of the lending institutions are already imposing much tougher new controls on solicitors. Last month Abbey National sent a circular to all solicitors, who wished to be on their panel, requiring those solicitors to give the bank the right to visit the practising address at any time during normal business hours and inspect the files on any transaction with which it is involved.

The mortgage application

One thing that surprises most people who are not familiar with the manner in which lending institutions work is the relative ease with which applications for large sums of money are processed with only the most basic check on the borrower's personal and financial references. I have personally been involved in cases where marked similarities between handwriting on the application form and on the employers' reference appear to have completely escaped the attention of lending clerks and managers whose job it was to check such matters. Based on my experience of mortgage fraud I believe lending institutions should consider the following as standard requirements:

> It is a good practice to make a point of interviewing all applications, particularly first time purchasers who apply for a mortgage.
>
> The application should be carefully checked for handwriting similarities with the references and if completed by someone other than the mortgage applicant (eg a packaging broker) a certificate should accompany it.

The proposed number of occupiers should be compared with the valuer's report on the question of the size and type of property. Many frauds I came across involved single people purchasing large houses which offered far more than normal accommodation. This check should be particularly done if the property is located in an area known as a bed-sit or DSS accommodation area.

Care should be taken to ensure that the purported salary is realistic when compared with the alleged age/experience/qualification/location of the applicant and the job.

A check should be made on the amount of the advance. If the advance is a very high percentage of the price or works out precisely as a multiple of the stated income or is the maximum which can be borrowed on the basis of stated income, caution should be exercised.

Employer's reference

The checking of employer's reference is particularly crucial. No lender should accept an unsolicited employer's reference accompanying the application form. Separate requests should always be made and the employer's letter confirming status should be on headed notepaper and not a photocopy.

Simple checks can be made on the employer's listing in the local telephone directory or with Directory Enquiries and, if listed, the telephone number and address of the reference should be confirmed. Failure to carry out this basic check is in my view "courting trouble". As one mortgage fraudster (now serving a three year prison sentence) confirmed, it is all too easy to establish a temporary office address. He told one reporter:

"you get an office somewhere and when the Building Society rings, you pretend to be their boss and say 'yes, so and so works here for x amount per week'. It's all done on trust".

The importance of establishing the longevity of the office accommodation is clear.

Proof of Identity

Proof of identity should always be demanded from the applicant such as current ten year passport, full UK driving licence, signed employer identity card from the known employers bearing photograph and signature or armed forces identity card. Certain

types of identification should not be accepted on their own; these include birth certificates, credit cards, national health cards, provisional driving licences and student union cards. I would recommend that at least two additional identity checks are taken, one reputable credit reference agency check and the other by way of either checking the electoral roll, a local telephone directory or obtaining a recent utility or community charge bill.

Whenever a broker is presenting a packaged mortgage the broker should be required to obtain a photocopy of the identification and valid confirmation that the originals have been checked.

What can be done if a fraud is discovered

Time does not permit any detailed exploration of the civil and criminal remedies which can be pursued when a mortgage fraud is discovered. Practical experience suggests that borrowers should immediately take steps to identify the extent of the problem in order to distinguish the "one off" fraudster from the larger and potentially more serious fraud ring. I would identify as suspicious any unexplained failure to meet repayments within the first six months following the mortgage. If the borrower has disappeared soon after the advance is made the implication is fairly clear and details of the transaction should be checked, preferably through a dedicated computer system, to try and identify common elements between frauds. In this way solicitors, brokers and valuers whose names consistently appear in suspect mortgage transactions can be quickly located and members of staff who might be involved can be identified.

Lenders pooling information

I referred, earlier, to the worrying case of two leading institutions who refused mortgage applications because of suspicions concerning the bona fides of the applicants but took no further steps. Britain's mortgage lenders already have a forum through which information could be exchanged and a step in the right direction was taken by the Council of Mortgage Lenders last year when they set up a register to record details of borrowers who have had their homes re-possessed voluntarily by the court dating back to 1989.

In addition, the big banks and building societies have been having a number of informal discussions on the question of pooling information about fraudsters, but I gather that these discussions have run into some difficulties on the question of the extent of the information that should be pooled. It is clear that financial institutions

do not like to publicise the fact that they have been defrauded and in some of the recent larger fraud rings a number of institutions have suffered substantial losses and are therefore competing for the same assets when pursuing their recovery actions. It remains to be seen whether any solution to these difficulties can be found, but clearly any pooling of information regarding suspect borrowers or professionals can only help to reduce the opportunity to defraud more than one lender and identify those who are actively pursuing careers in mortgage fraud.

The discovery of mortgage fraud and resulting claims of the type I have discussed are likely to have serious implications for the financial and insurance industries - at least while there is a static or falling property market and then for several years thereafter as the problems are sorted out. The number of systematic frauds could well decline, as the flat and falling market fails to offer the incentives required by systematic fraudsters, but as more routine checks are put in place it is likely that the commission of mortgage fraud will become more sophisticated. It only by greater awareness of the problem, the introduction and maintenance of strict lending procedures and tighter regulation on those involved in mortgages from a professional stance that lenders and their insurers will be able to keep ahead of the fraudsters.

3. MARINE INSURANCE
by Richard J. Sayer, Ince & Co.

It is a privilege to be with you all at this your seventh annual conference, and to have been asked to speak on the subject of marine fraud.

I have over the last thirty years practised marine fraud with some regularity, always I hasten to add on the side of the angels - the insurers. I must therefore begin by apologising to all those of you here who are fraudulent shipowners or fraudulent cargo owners - I am somewhat prejudiced and I may not therefore give due weight to your point of view during the next 20 minutes.

Now you have a distinguished panel of speakers to talk about insurance fraud - I don't wish to cut across anything they will be saying so I will confine my remarks about marine fraud to the *wet* aspect of that subject. Marine insurance can be put broadly into 2 categories - dry - which involves documentary and cargo fraud; and wet - involving casualties to vessels. As part of my practice as a maritime lawyer I was a member of a team of investigators who looked at over 60 cases of total loss of ships in the South China Sea in the late 1970's.

After a four month investigation we found that at least 28 vessels had sunk in highly