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November 26, 2014

Secretary
Financial and Consumer Services Commission
85 Charlotte Street, Suite 300
Saint John, NB E2L 2J2

Comments on the New Brunswick rules regarding Mortgage Broker Licensing and Ongoing Obligations

On behalf of the Mortgage Brokers Association of BC (MBABC), I would like thank you for affording our association with an opportunity to make submissions concerning the Financial and Consumer Services Commission's proposed rules regarding "Mortgage Broker Licensing and Ongoing Obligations". The new legislation and proposed rules appear to be well crafted and create a forward thinking licensing regime for mortgage brokers in New Brunswick.

By way of background, the MBABC is a 25 year old professional association which represents mortgage brokers and many private mortgage lenders in British Columbia. Regulatory oversight of mortgage brokers in BC was implemented with the enactment of the BC *Mortgage Brokers Act* in 1972, which was at that time an innovative piece of legislation. The MBABC has therefore accumulated a considerable depth of knowledge of mortgage broker regulation and mortgage broker practice. We can offer the following comments for your consideration concerning New Brunswick's proposed rules.

Exemptions from Mortgage Broker Licensing – section 2 – Bank Brokers

Sections 2(a) and (c) exempt financial institutions and their employees from the requirements to comply with the *Mortgage Brokers Act* (the "MBA"), which includes the requirement to obtain licensing under the MBA. This exemption may be worded too broadly and capture mortgage brokering activity that falls clearly under provincial jurisdiction – not federal and not under the *Bank Act*.

The *British North American Act* of 1867 (now called the *Constitution Act*, 1867) defines Canada's federal structure by determining the jurisdiction or areas of authority to be exercised by both the federal government and the individual provincial governments.

The federal government has control over all matters not coming under provincial control, in addition to a list of specified areas, including “banking”. While the provincial legislatures have jurisdiction over a list of specified areas which include property and civil rights. The property and civil rights powers have been broadly interpreted to provide the provinces with authority over professional trades and consumer protection issues. Mortgage broker regulation is therefore a provincial matter by virtue of the provinces power to regulate matters relating to property and civil rights within their provincial borders.

“Banking” is not the same as “bank business”, and in many cases banks are engaging in non-banking bank business that falls within provincial jurisdiction, such as selling insurance or mutual funds. Another example would be that of mortgage brokering. Bank mortgage brokering occurs where the bank employee does not facilitate a loan with the bank, but rather brokers a mortgage deal with a third party lender, such as a trust company, mortgage investment corporation or other private lender. In addition, we are of the view that bank mortgage brokering includes dealing in mortgages under a name other than the proper name of the bank, and bank employees representing themselves to the public as mortgage brokers or mortgage advisors.

The Supreme Court of Canada has just rendered a long awaited and ground breaking decision which provides guidance on this issue. In the case of *Bank of Montreal v. Real Marcott (*and two other cases), a class action suit was brought against the bank for failing to disclose exchange fees on credit cards as credit charges, as required by Quebec consumer protection legislation. The bank argued that the Canadian constitution gave the federal parliament exclusive jurisdiction to regulate banks. However, the court decided that Quebec’s consumer protection legislation is “constitutionally applicable and operative” to banks.

We can easily apply the principles set out by the Supreme Court in Marcott to the case of bank brokering, and conclude that exemptions from mortgage broker licensing for bank employees, who arrange third party mortgages, are unconstitutional. It puts control over bank brokering within federal control, and thereby infringes on an area of provincial jurisdiction.

We therefore recommend that you clarify the proposed exemption for banks and their employees by ensuring that the exemption does not apply to the following:

- The act of brokering mortgages for borrowers with third party lenders which are not the financial institution;
- Dealing in mortgages under a name which is not the proper name of the financial institution; and
- Employees of financial institutions who represent themselves as advisors or brokers.

<u>Exemptions from Mortgage Broker Licensing – section 3 - Referrals</u>

Sections 3(a) and (b) exempt persons from the requirement for mortgage broker licensing if they are engaging in referral activity and satisfy the criteria laid out in these sections. Persons who make incidental mortgage referrals, such a realtor who recommends a mortgage broker to a purchaser, should not be captured by a requirement to obtain mortgage broker licensing. However, entities and individuals who actively solicit mortgage referrals as a business should not be exempt from mortgage broker licensing.

Businesses which specialize in mortgage lead generation or providing mortgage referrals to brokers for a fee have exponentially proliferated over the last ten years. A bulletin (MB10-004) from the BC FICOM website describes mortgage lead generation as involving "an entity or individual gathering lists of potential mortgage borrowers, who are considered to be "mortgage leads". The lists of mortgage leads are then sold to mortgage brokers, who may contact the individual leads for the purpose of attempting to arrange mortgage financing for them. The lists of potential mortgage borrowers are often generated through the internet by setting up a website which may provide mortgage information or mortgage advice and providing a simple form of mortgage application. The application data is gathered by the mortgage lead generator and then forwarded to the mortgage broker. Mortgage leads may also be generated over the telephone by telemarketers contacting persons and enquiring about their interest in obtaining a new mortgage or refinancing a current mortgage, in addition to gathering personal and financial information from the potential borrower."

Mortgage lead generators or mortgage referral businesses often resemble mortgage brokers and lenders. In many cases, it is impossible for the public to differentiate them from a broker. We therefore recommend that section 3 be revised to ensure that individuals or entities which actively solicit mortgage referrals not be exempt from the requirement to obtain mortgage brokering licensing.

Section 3 – Education

This section provides that applicants for licensing who pass a licensing course can apply for licensing up to three years following the date of their course completion. This is a significant length of time and they are likely not to remember many of the details of their course material. For this reason, in British Columbia, registration applicants must apply for registration within one year of passing the qualification course. We recommend that you shorten the time period for licensing application from three years to significantly less than three years, such as one year.

Section 14 – Unlawful Transactions

This section prohibits a mortgage brokerage from acting for a client if it "has reasonable grounds to believe" that a mortgage or investment in a mortgage is "unlawful". This section places a very high burden on mortgage brokers and it requires them to possess legal knowledge in order to assess the lawfulness of a transaction, which they are unlikely to possess. Whether a mortgage transaction is lawful or not is a matter within the expertise of a lawyer. The commission may therefore want to consider using alternate language in this section, which could even encompass misconduct which is

broader in scope than “unlawfulness”. For instance, it could borrower language from the BC *Mortgage Brokers Act*, which prohibits mortgage brokers from being “a party to a mortgage transaction that is harsh and unconscionable or otherwise inequitable”. In addition, most mortgage brokerages are corporate entities, and it is not clear how they can possess beliefs or grounds to believe. You may therefore want to consider placing the burden in this section on the controlling mind of the mortgage brokerage, which would be the mortgage broker.

Sections 15 and 16 – Borrower’s Legal Authority and Accuracy of Mortgage Application

Section 15 requires a mortgage brokerage to advise a lender if it possesses a reason to doubt the legal authority of a borrower to mortgage a property. Again, it is not clear how a corporate entity can have the capacity to “doubt”, and you may wish to consider changing the burden in this section to the mortgage broker. In addition, the burden is very high – requiring the advice to be given if there is “a reason”. A clearer and more practical application of the burden could focus on “actual Knowledge” of a borrower’s lack of authority to enter into mortgage. We would recommend that section 16 be similarly amended for the same considerations.

Section 22 – Disclosure to Private Investors

The most critical information for any mortgage investor is the loan to value (LTV) ratio. Calculating the LTV requires investigating the state of title and determining the outstanding balance or the maximum potential balance (in the case of running accounts or draw mortgages) of financial charges which will remain on title and rank in priority to the mortgage investment. We recommend that section 22 be amended to require the mortgage broker to state in a disclosure to private investors:

- Which financial encumbrances will remain on title;
- The priority of remaining financial encumbrances;
- The priority of the mortgage which is the subject of the disclosure;
- The outstanding balance or maximum potential balance (whichever is higher) of all remaining financial encumbrances; and
- The LTV of the mortgage which is the subject of the disclosure.

Section 26 Advance Fees

This section prohibits a mortgage brokerage from charging or receiving fees or other remuneration from borrowers until the mortgage has been funded and registered in the applicable land title office. The purpose of any prohibition against taking advance fees is to prevent advance fee fraud, wherein a fraudster will promise to loan money in return for an upfront fee. The fraudster then pockets the advance fee with no intention of funding the loan. However, an outright prohibition against advance fees could potentially cripple the mortgage broker industry in New Brunswick.

We would suggest that New Brunswick adopt a more balanced approach to the issue of advance fees which takes into account the mortgage broker’s right to be compensated

for valuable service provided to the public. The challenge for many mortgage brokers is that they may be reluctant to take on difficult mortgage clients, when their fee is contingent on their application actually being approved and funded. Often mortgage files require many hours of preparation, document management and negotiation. Sometimes mortgage commitments are obtained by mortgage brokers after they have invested significant amounts of time into the file, but the client will eventually opt for alternative financing or decline the offered financing – this can happen even at the last minute, just prior to closing . Under the wording of section 26, mortgage brokers will have no way of collecting fees when there is never any mortgage funding from which to deduct the fee.

Most professionals, including lawyers, accountants and realtors are able by contract to negotiate advance fees. Lawyers, for example, commonly ask for a retainer of funds from a client, which are kept in their trust account and withdrawn only when the services and an account have been rendered.

In Ontario, the Regulations to the *Mortgage Brokerages, Lenders and Administrators Act* provide that "If the principal amount of a mortgage is $300,000 or less, a brokerage shall not require a borrower to make, and shall not accept, an advance payment or deposit for services to be rendered or expenses to be incurred by the brokerage or any other person." Advance fees are therefore permitted to be charged by mortgage brokers in Ontario for residential mortgages with a principal sum of over $300,000.

In Alberta, section 71 of the *Real Estate Act* Rules places restrictions on the collection of an advance fee for assisting an individual in obtaining a mortgage from a lender. This rule applies to a mortgage where the borrower is an individual who enters into a credit arrangement primarily for personal, family or household purposes. It prohibits collecting a fee from such an individual until the lender has provided written confirmation to fund the mortgage to the borrower, has provided an initial disclosure statement and at least two business days have passed since the disclosure statement was received (or the individual has waived the time period for its delivery in accordance with the *Fair Trading Act*). In Alberta then, mortgage brokers are entitled to charge fees in advance of mortgage funding if a mortgage commitment has been obtained and cost of credit disclosure rules are followed.

Section 26 prohibits mortgage brokerages from receiving "other remuneration" until the mortgage transaction is closed. The wording here could prevent brokerages from collecting costs in the course of a transaction to cover out of pocket expenses such as appraisal fees. This provision potentially creates a substantial risk to the mortgage broker who should not have to bear any of the borrower's costs to facilitate the mortgage transaction.

Commercial mortgage transactions generally unfold much differently from conventional residential transactions, in that fees are paid by the borrower to the brokerage at the time a commitment is provided to the borrower. The rationale for this is that commercial transactions are more complicated and time consuming than residential transactions, and brokers need to secure their fee at the time they complete their work for a client, which is at the time of obtaining a commitment and not later, at the time of funding. However, section 26 appears to apply to both residential and commercial mortgage

transactions. Not only are commercial borrowers generally more sophisticated than their residential counterparts, advance fee scams mostly target more vulnerable residential borrowers. The advance fee limitation will therefore have a severe impact on commercial mortgage transactions without any apparent public protection benefit.

Accordingly, we recommend that section 26 be amended to permit:

- The charging of fees and costs at any stage of a commercial transaction;
- The charging of costs at any stage of a residential transaction; and
- The charging of fees upon the delivery of an acceptable mortgage commitment for residential transactions.

We further recommend that in order for fee agreements to be enforceable that they be reduced to writing and that the brokerage be duly licensed under the MBA.

Wind up Reports

You may wish to require mortgage brokerages which cease to carry on business in New Brunswick to file a wind up report, which describes how outstanding files, mortgage loans and any trust monies have been concluded, transferred or otherwise dealt with.

Pooled Trust Account Interest

Interest which is accumulated from a pooled trust account does not belong to the mortgage brokerage, yet it is practically impossible to disperse amongst the beneficiaries of the pooled trust. You may wish to create a section which specifies how interest from pooled trust accounts is to be dispersed.

Thank you for the opportunity to make comments on your proposed rules. If you wish to discuss any of the comments further, please feel free to contact me.

Yours truly,
THE MORTGAGE BROKERS ASSOC. OF BC

Samantha Gale, CEO