

REVIEW OF NEW AND PROPOSED LEGISLATION AFFECTING MORTGAGE LOAN TRANSACTIONS

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The disclosure in Manitoba of questionable loan practices in respect to Real Property mortgages reflects a situation that is not peculiar to Manitoba. Many of the larger urban areas in the United States and Canada which have experienced a population explosion and that inevitable building boom can already testify to these practices as revealed by "The Tallin Commission on Real Property Mortgage Loan Transactions".

These revelations shocked the citizenry of Manitoba only because the prairies always tend to share in prosperity, and its attendant evils, at a somewhat later date than the other more prosperous and affluent regions of North America.

For proof that these practices are not unique to Manitoba one has only to look back to the American Senate hearings on organized crime to see how the criminal element has invaded the fields that were once thought to be the exclusive domain of respectable lending institutions. However, if we are somewhat slow to feel the impact of prosperity, we can also gain an advantage from this in that we have as our guide, legislation passed by other jurisdictions which have already encountered the problems of prosperity and attempted to solve them by new legislation.

The Tallin Commission did three things: it confirmed that these questionable practices do in fact exist in Manitoba; it reviewed the present state of the law in Manitoba with respect to these types of loan transactions; it made recommendations for new legislation to combat these practices.

In respect to the first two points stated above, nothing new need be added other than to say that the law of Manitoba was inadequate to deal with this problem. The last point dealing with the matter of new legislation is more contentious, and from the lawyers' point of view, is by far the most important aspect of the report.

The actual terms of reference of "The Tallin Commission"¹ directed the Commissioner:

. . . to inquire into and report on all matters connected with real property mortgage loan transactions in respect of which representations had been made to the Attorney-General or might be made to the Commissioner where the terms are alleged to be harsh and unconscionable, and to make recommendations upon the method by which relief against such transactions may be

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1. See Appendix I, Page 23, of "The Tallin Commission on Real Property Mortgage Loan Transactions" for terms of reference in full.

obtained and the sufficiency for that purpose of certain proposed Acts of the legislature, namely; an Act for Relief from Certain Unconscionable Transactions, an Act requiring Registration of Real Estate Brokers and Real Estate Agents, and an Act requiring Registration of Mortgage Brokers.²

The Commission's terms of reference were later broadened to include "loan transactions arising in whole or in part from work done or material supplied for improvements to real property and not secured by a real property mortgage", but which were secured by a promissory note payable by monthly instalments.³

The first point which the Commission was charged with under its terms of reference was to examine whether certain real property mortgage loan transactions were harsh and unconscionable. The second point dealt with by the Commission under its terms of reference was that if certain transactions were harsh and unconscionable, was the legislation proposed by the legislature adequate to relieve against these harsh real property mortgage transactions.

As to the first point under the terms of reference, the Commissioner's report left little doubt that there were a great many questionable transactions which fell into this category. The report of the Commissioner states that he heard 38 cases involving this type of transaction, the majority of which, to say the least, were hardly advantageous to the borrower. The Commission was of the opinion that the cases investigated were only a small sampling of the practice as it existed, and that these loan transactions were much greater in number and extent than was indicated by the people who came forward to complain to the Commission. The Commissioner felt that this reluctance to appear before the Commission might be attributed to the publicity given to the hearing by the newspapers. One can understand a person's reluctance to have his financial difficulties made a matter of public record, not to speak of the exposure of his financial ignorance, but even so, when given an opportunity for relief from these catastrophic financial burdens, many of those affected failed to take the opportunity given them by the Commission. One can only surmise that whatever legislation is passed, people will still be reluctant to take advantage of the relief offered by it.

The benefits provided by the legislation for the relief of these unfortunate persons is at the option of the person complaining of the

2. See Page 5 of "The Tallin Commission on Real Property Mortgage Loan Transactions".

3. It is interesting to note that the words used by the Commission "work done or material supplied" bear a close resemblance to the wording used in Section 15(1)(b) of the Mechanics Lien Act, Cap. 157, R.S.M. 1954. What in actual practice did happen was that the holders of these promissory notes would register a Mechanic's Lien against the title based on the promissory notes. Since a Lien does not expire until two years after "the work or service has been completed or materials have been furnished or placed, or the expiry of the period of credit where the period is mentioned in the claim of lien registered" (Sec. 22, Mechanic's Lien Act) it has the effect of acting as an encumbrance or equitable mortgage. It is quite true that the registered owner could force the lien holder to take action under the lien, but this would do him little good in view of the fact that the promissory note was still held by the lineholder. The use of the Mechanic's Lien Act in this way affords the lender the opportunity of securing his debt without the necessity of registering a mortgage and thereby, disclosing the unconscionable nature of the transaction. This is clearly an abuse of the Mechanic's Lien Act. The Act was never intended to provide an instrument whereby a lender could use it as a method to protect an unconscionable transaction and yet it appears that the Act clearly serves this purpose.

harsh and unconscionable transaction. Unlike the criminal law, where the state can, and does, initiate the action, the individual who alleges the unconscionable loan, will have to hire his own counsel and, if necessary, pursue the complaint in the courts himself. Undoubtedly many persons will continue to struggle along, paying off these mortgages without seeking relief, either because of ignorance of the new legislation, or because of their fear of becoming involved in a law suit that will only add to their already substantial financial burdens.

The Commissioner sets this view out in his report when he says:

In your Commissioner's opinion it would not be feasible or even possible to enact legislation which would protect everyone against the possibility of becoming involved in transactions of the type which have been investigated. Legislation would, as it were, only deal with symptoms and leave causes untouched. Most of the persons who become enmeshed in difficulties of this sort have already, through lack of good judgment and foresight become so financially involved that nothing short of an assignment in bankruptcy or a voluntary adoption of a markedly lower standard of living will get to the root of their troubles and provide a workable cure. An unwillingness to accept either of these unpleasant alternatives drives them to a moneylender when they should go to a lawyer. The moneylender at best offers them a form of temporary relief that only serves to prolong their suffering. It is, of course, unrealistic to expect them at this stage to incur the anticipated cost of seeking legal advice, when probably one of the reasons for their plight is that they neglected to do so in the past. Statutory remedies, however effective, are not fully automatic or self-administering, and those who are to enjoy their benefits must be willing to seek the assistance of those trained to administer them. Even if such assistance were available without cost to those needing it, they would still have to take the initiative in asking for it. This, many who need it most, will not do.

Again, it must be realized that measures stringent enough to protect a small minority of persons against the results of their own ignorance, folly and stupidity might impose intolerable obstacles on the conduct of ordinary business transactions by the large majority of persons who act with normal degrees of caution, wisdom and foresight.⁴

The second point the Commission was asked to examine was the adequacy of the proposed new legislation. This involved the examination of two completely new statutes: An Act to provide for Relief from Certain Unconscionable Transactions,⁵ An Act requiring this Registration of Mortgage Brokers,⁶ and also a look at the Real Estate Brokers Act⁷ which has been extensively rewritten. This latter Act was previously The Real Estate Agents and Salesmen Act.⁸

The Unconscionable Transactions Relief Act has as its model the English Money Lenders Act⁹ and the Ontario Unconscionable Transactions Act.¹⁰ The Manitoba Act follows the Ontario Act word for word, with two important exceptions.

4. Pages 20-21 of The Tallin Commission on Real Property Mortgage Loan Transactions.

5. S.M. 1964, second session, Cap. 13.

6. S.M. 1964, second session, Cap. 6. Proclaimed in force April 1, 1965.

7. S.M. 1964, second session, Cap. 9. Proclaimed in force April 1, 1965.

8. R.S.M. 1954, Cap. 213.

9. The English Moneylenders Act, 1900 (63 & 64), Vict. C. 51, Amended (17 & 18), Geo. 5, C. 21.

10. The Unconscionable Transactions Relief Act, R.S.O., 1960, C. 410.

In the Manitoba Act, Section 3 reads:

Where, in respect of money lent, the court finds that, having regard to the risk, and to all the circumstances at the time the loan was made, the cost of the loan is excessive *or* that the transaction is harsh *or* unconscionable the court may . . .

In the Ontario Act the similar Section 2 reads:

Where, in respect of money lent, the court finds that having regard to the risk and to all the circumstances, the cost of the loan is excessive *and* that the transaction is harsh and unconscionable, the court may . . .

The Manitoba Act, therefore, technically and theoretically, gives the court a broader base upon which to reopen a transaction and revise it if the court wishes to do so. The person seeking relief here need only prove one of three things: that the cost of the loan is excessive; that the loan is harsh; or that the loan is unconscionable. I think that we can safely say that if the court made a finding of harshness this would be equivalent to saying the loan is unconscionable. Similarly, if the court found that the cost of the loan was excessive, then, undoubtedly, it was harsh and unconscionable.

In reality, the courts tend to look at the overall circumstances under which the loan was made, and if satisfied that it was not reasonable in the circumstances, then it would be excessive, and therefore harsh and unconscionable. The courts seem to prefer to make their decision on the basis of the overall context of the Act rather than to try to give a specialized meaning to individual words or to particular sections of the Act.

This was best put by Lord Justice Romer in the case of *Poncione v. Higgins*¹¹ when he said:

In his Lordship's opinion it would be mischievous to formulate what conduct on the part of a moneylender was "harsh and unconscionable" within the words of the Act. He would content himself with saying that the Judge should in every case consider the various circumstances under which the loan had been effected and the terms of the loan, such as the rate of interest, the security, and so forth.

Again, in the same case, Lord Justice Hardy said:

It was possible that the interest might be deemed excessive, and yet the transaction might not be deemed harsh and unconscionable. And it was possible that the interest might be deemed so extravagantly excessive as alone to satisfy the Court that the transaction was harsh and unconscionable. It was obviously not possible to lay down a fixed general rule as to rate of interest. The circumstances of each case must be considered, including the necessities of the borrower, his pecuniary position, the presence or absence of security, the relation in which the moneylender stood to the borrower, and the total remuneration derived by the moneylender from the whole transaction.

11. *Poncione v. Higgins*, (1904), 21 T.L.R., 12.

And, finally, in the most recent case in Ontario of *Moorehouse et al v. Income Investments Ltd. et al.*,¹² Judge Sweet of the County Court of Wentworth said:

I do not think that an attempt should be made to set out here firm and unelastic definitions of what constitutes unfair advantage or as to what is "harsh and unconscionable". The minds of many are often facile in the devious and agile in ingenuity for its accomplishment. It would, I think, be futile, perhaps even dangerous, to attempt to establish total safeguards in the hope that they would be effective against all selfishness and chicanery. Invention often adds new oppression to the old.

Furthermore, the cost of a loan in a transaction between some men and under some circumstances might be fair and reasonable but the same cost in transactions between other men and under other circumstances might be harsh and unconscionable. Then, too, what might be an excessive cost at one time might be a reasonable cost at another. Each case must be decided upon its own facts and against its own background.

The Manitoba Act differs from the Ontario Act in another important essential. When the Manitoba Act was first passed it followed the Ontario Act in respect to the rights of a bona fide assignee or holder for value.¹³ The assignee or holder for value without notice might not be subject to the Act as it originally stood. This could have had the effect of depriving the mortgagor of any benefits under the Act if the purchaser of the mortgage was a bona fide purchaser for value without notice.

Dean Tallin in his report recommended that this be changed:¹⁴

It is possible that because the mortgagee and assignee were different legal persons, a court, despite the closeness of their association might hold that the assignee took without notice of any of the circumstances surrounding the original transaction. It is for the purpose of preventing the mortgagor from being deprived by the assignment from any remedies to which he might otherwise have been entitled . . .

The amendment that followed from the Commission's recommendation was that where an assignment is made, either before or within a two-year period after the money lent has been disbursed "the assignee shall *not* be deemed to be an assignee for value without notice". However, if the assignee receives an acknowledgement from the debtor in which the debtor acknowledges that he is aware of the cost of the loan, to whom the proceeds of the loan have been disbursed and the amount that he received after such costs and disbursements were paid then the debtor is estopped from denying that the assignee is a bona fide assignee or holder for value without notice. The acknowledgement must be taken before a solicitor who is entitled to practise in Manitoba who certifies that he has explained the meaning, purpose and effect of such an acknowledgement to the debtor. The acknowledgement must be taken at least forty-eight hours after the money lent has been wholly disbursed.

12. *Moorehouse et al v. Income Investments Ltd. et al.*, [1966] O.R. 232.

13. See Section 6, Cap. 13, S.M. 1964, second session, and See Section 7, Cap. 410, R.S.O. 1960.

14. The Tallin Commission, Page 22.

In the "Tallin Commission Report", Dean Tallin recommended that the two years should run from the date of registration of the mortgage. The amendment, however, specified a two-year period following the disbursement of the mortgage proceeds rather than following the Land Titles registration.¹⁵ Had the Commission's recommendation been followed, it would have had the effect of making an assignee subject to this "two year rule" regardless of how many years had elapsed since the mortgage had been executed. Since the proceeds of a mortgage are usually disbursed within a relatively short period after registration, it would have made little difference if the time had been made to run from the registration date rather than the disbursement date. If the Commission's suggestions had been followed, a further benefit would have accrued in that the mortgagee would be compelled to register his mortgage. This would be a desirable end in itself in view of the fact that many mortgages are not registered but are protected by way of a Caveat registered in the Land Titles Office. The exact terms of the mortgage are, therefore, not a matter of public record, but remain hidden from public scrutiny.

The mortgagee, in a harsh and unconscionable transaction will, therefore, still be able to conceal the terms of the transaction from the public and it seems that the legislators might have provided a further safeguard by carrying the amendment one step further and thereby affording the public even greater protection.

Generally, the legislation as it now stands appears to be adequate for the purpose for which it was intended, that is, to give an opportunity to those less affluent members of our society who have made a bad bargain to have it remade by the courts in terms that are less oppressive. We must, however, remember, that in the words of the Commissioner; "statutory remedies, however effective, are not fully automatic or self-administering and that the onus is still on those who have made a bad bargain to seek the relief as provided by the Act." The Act is only intended to provide machinery whereby the courts can make a transaction that was unconscionable into a transaction that is fair and reasonable. The Act is not intended to prevent such transactions from being made at all.

Before passing from the Unconscionable Transactions Act, we should note that the Supreme Court has ruled that this Act is within the powers of the province. Mr. Justice Judson made this quite clear in the case of *A.-G. v. Barfried Enterprises Ltd.*,¹⁶ where he said that:

In my opinion, it is not legislation in relation to interest, but legislation relating to annulment or reformation of contracts on the grounds set out in the Act, namely, (a) that the cost of the loan is excessive, and (b) that the transaction is harsh and unconscionable. The wording of the statute indicates that it is not the rate or amount of interest which is the concern of the legislation, but

15. S.M., 1965, Cap. 87.

16. *Attorney General for Ontario v. Barfried Enterprises Ltd.*, (1964) 42 D.L.R. (2d), 147.

whether the transaction as a whole is one which it would be proper to maintain as having been freely consented to by the debtor. If one looks at it from the point of view of English law it might be classified as an extension of the doctrine of undue influence . . . The theory of the legislation is that the Court is enabled to relieve a debtor, at least in part, of the obligations of a contract to which in all the circumstances of the case he cannot be said to have given a free and valid consent. The fact that interference with such a contract may involve interference with interests as one of the constituent elements of the contract is incidental. The legislature considered this type of contract as one calling for its interference because of the vulnerability of the contract as having been imposed on one party by extreme economic necessity. The Court, in a proper case, is enabled to set aside the contract, rewrite it and impose the new terms.

The Commission recognizing the fact that the Unconscionable Transaction Relief Act did not prevent these questionable transactions from being entered into initially suggested certain changes to the Mortgage Act which are presently being studied by the Manitoba Legislature with a view to implementing these recommendations.

The Commissioner recommended that there be a declaration or affidavit by the Mortgagee setting out to whom the proceeds were paid if these proceeds were paid to anyone other than the mortgagor or his agent or assignee and that the "cost of the loan" as defined in the Unconscionable Transactions Relief Act under Section 2(a) be also set out in this affidavit. He further suggested that a "practicing solicitor" should certify that he has read over and explained this affidavit or declaration of the mortgagee to the mortgagor and that the mortgagor acknowledges that he understands the contents of the affidavit or declaration.

The Commissioner takes aim at lawyers when he recommends that "No solicitor should act for both the lender and the borrower in a mortgage transaction in which the real cost of the loan to the borrower is in excess of 10 per cent." To further ensure that there can be no doubt as to the intention of his recommendation he suggests that in the certificate the solicitor gives in connection with the loan transaction he should make a statement that he has only acted for the mortgagor in the transaction.

As a final precaution the report suggests that the cost of the loan be expressed as a rate of interest and referred to as the "real rate of interest" and it be displayed in a prominent place in the mortgage so that there can be no question as to what the real cost of the loan is to the mortgagor.

In order to exempt the traditional corporate lending institutions the report recommends that where the "real rate" of interest does not exceed 8 per cent then an exception to these requirements may be made. This has the effect of relieving institutions such as Central Mortgage and Housing Corporation, insurance companies and trust companies from having to give such a declaration.

The Bill that was introduced into the House to amend the Mortgage Act restricts the requirement of an affidavit or statutory declara-

tion to those cases where the money is being disbursed to persons other than the "Mortgagor or his agents or assignees".¹⁷ The Commission's recommendation made this affidavit or statutory declaration a condition of every mortgage except where the real interest rate is 8 per cent or less.

The proposed bill drops the recommendation that a practising solicitor give a certificate that he explained the transaction to the mortgagor and further that he acted only on behalf of the mortgagor in the transaction. Finally, the proposed bill extends the definition of the "cost of loan" by adding inspection and legal fees to the definition already given to this term under the Unconscionable Transaction Act.

Some members of the legal profession object to the amendment on the grounds that in order to protect a minority of people the amendment will have the effect of increasing costs for the majority of borrowers. This minority, as Dean Tallin points out, got into trouble because of their own ignorance and folly, and in our zeal to protect this minority we may be penalizing "a majority of persons who act with normal degrees of caution, wisdom and foresight."

The Legislative Committee of the Manitoba Bar Association took exception to the proposed bill on five grounds.¹⁸ The majority of these objections were based on technical grounds, with the real contentious issue being the extended definition of "costs of the loan". The Bar Association Legislative Committee takes the stand that the lawyer cannot estimate the costs of the loan at the outset of the transactions. Some costs occur during the course of the transactions, but after the mortgage has been registered. The Association also suggests that where the normal inspection or valuation costs do not exceed $\frac{1}{2}$ of the 1 per cent of the loan or \$50, whichever is less, these should also be excluded. Legal fees, the Association contends, "should also be excluded since they are subject to taxation by an officer of the court, and if a borrower desires to have a legal bill reviewed there is ample and effective procedure now for dealing with same".

The Bill in its original form was put over by the legislature for further study and to hear additional representation before the final draft is presented to the House for approval and at the time of this article that is where the matter stands.

The Commission was also asked to consider the sufficiency of the Real Estate Brokers and Real Estate Agents Act and an Act requiring Registration of Mortgage Brokers. The Commissioner dealt very summarily with these acts by saying that these Acts will achieve the purpose for which the legislation was enacted. Both of these Acts are regulatory and are intended to control those people who deal with the

17. Bill 119—An Act to amend The Mortgage Act.

18. *Manitoba Bar News*, June, 1965, Vol. 35, No. 12, p. 338.

sale and financing of Real Property. The purpose of both these Acts is to provide a means whereby authorities can weed out unscrupulous Real Estate Agents and Mortgage Brokers and hopefully to prevent "shoe-string" operators from opening up shop, making a "fast buck", and then disappearing, leaving behind a trail of financially ruined and dispossessed homeowners.

The purposes for which these Acts were intended and how well their purposes are achieved will depend in large measure on how well the responsible authorities administer these Acts and use the legislation that is provided to prevent these shady operators from gaining a foothold in the legitimate real estate market. This, in turn, will depend on whether the citizen will come forward to complain to the authorities responsible for the administration of these Acts.

In my opinion, the Tallin Commission achieved the purposes for which it was established. It gave its stamp of approval to the proposed new government legislation and in addition recommended new legislation and amendments to already existing legislation in order to provide relief against harsh and unconscionable real property mortgage transactions. Moreover, it served an even more useful purpose in that it informed the general public of a practice which was little known to them before the establishment of the Tallin Commission. Outside of those people who normally have a close connection with the real estate market I think the general public was blissfully unaware of a practice that had become quite widespread well before the Tallin Commission and the news media exposed these questionable practices. The effect of this general public knowledge is not only to encourage much needed legislative reforms, but also to make those people who deal with real estate and its allied financial transactions, to become much more guarded in their professional conduct and practices. Professional bodies in particular are always very conscious of their public image and are quick to respond if this image becomes tarnished in the public mind. Most of these bodies are self-disciplining and self-regulating and whether they continue to be so depends in large measure on how well they can keep their image untarnished in the public eye.

The problems examined by the Tallin Commission represent only one small aspect of a much greater problem, the complexities of which pose an even greater dilemma for our legislatures and lawyers. The real question raised by the Tallin Commission is the extent to which we as a society, are prepared to go in rewriting private contracts made by freely consenting adults. Implicit in its report is that the state can only provide limited protection to the average citizen. If the state attempts to supervise all private contracts made between its citizens, the ultimate result could be that the state will be entering into contracts with itself. This, of course, is an extreme position, but nevertheless in our desire to protect people from themselves and their own

stupidity, we can find ourselves in the position where the state, by legislation is always the third unseen party to the contract. The effect of this on the normal business and commercial world is to make it even more difficult and expensive for the average citizen to raise badly needed capital and hence to drive him in desperation to seek this capital from sources less reliable and less honest than traditional commercial sources. The question we must then ask ourselves is how far are we willing to go, and, as Dean Tallin said in his report:

It must be realized that measures stringent enough to protect a small minority of persons against the results of their own ignorance, folly and stupidity might impose intolerable obstacles on the conduct of ordinary business transactions by the large majority of persons who act with normal degrees of caution, wisdom and foresight.

The answer to this question lies somewhere between the two extremes. The citizen must still essentially make his own contract but the state must even up the odds by seeing that those contracts do not transcend the traditional rules of what our society considers to constitute a conscionable bargain.

