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February 28th 2014

Jane Pearse

Director, Financial Institutions Division

Financial Sector Policy Branch

Department of Finance Canada

15th Floor, East Tower

140 O'Connor Street

Ottawa, ON

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RE: Canada's Financial Consumer Protection Framework: Consultation Paper

By Email: code.consult@fin.gc.ca

Dear Ms. Pearse,

In response to the federal government's call for consultation on December 3rd, 2013, The Canadian Real Estate Association (CREA), on behalf of its over 100,000 members, is pleased to submit comments to help strengthen Canada's financial consumer protection framework.

While CREA commends work done so far by the government and other stakeholder groups to improve consumers' awareness and understanding of financial aspects of the home buying process, we believe further action is needed to truly protect consumers. Indeed, according to Canadian Mortgage and Housing Corporation (CMHC) research published in 2013, "less than 50% of First-Time Buyers totally agree that they got the best mortgage deal for their needs; that they had a good understanding of mortgage options; and that the process of getting a mortgage was easy and straightforward. Qualitative research also indicates that they desire more complete and accessible information on a variety of topics."

CREA would therefore like to submit **four recommendations** to improve the current practices and protect consumers. These recommendations concentrate on the necessity to provide consumers of financial products with improved disclosure when dealing with Federally Regulated Financial Institutions (FRFIs). By tackling the degree and uniformity of disclosure, these measures would not only better

provide critical information to consumers, but also place consumers in a better position to evaluate their options across institutions.

1. First, steps must be taken to clarify the conditions of mortgage pre-approvals. This includes making explicit instances of conditional approval and prohibiting the advertisement of pre-approval amounts as a determination of what a consumer can afford.
2. Second, mortgage pre-payment penalty provisions must be more accessible before a consumer signs a mortgage contract. Specifically, general conditions must be displayed prominently on an FRFI's website. In addition, prepayment provisions of a mortgage should be proactively disclosed at the time of pre-approval and when signing a mortgage contract. If any provisions are different than what was previously presented, these differences must be brought to the consumer's attention. Disclosure of this prepayment information should not be merely upon request.
3. Third, the use of plain and not misleading language, as per the Financial Consumer Agency of Canada (FCAC) definition, should be mandatory on all FRFIs' disclosures with customers and be accompanied by examples to illustrate certain conditions.
4. Fourth, compliance with the Consumer Code should be mandatory, with the mandate of the FCAC encompassing more stringent enforcement through enhanced, scheduled monitoring and reporting.

Summary of Policy Recommendations:

Recommendation #1 – The conditions of mortgage pre-approvals must be clear. Changes to existing practices include making explicit instances of conditional approval and prohibiting the advertisement of pre-approval amounts as a definitive determination of what a consumer can afford.

Rationale:

Mortgage pre-approval arrangements are an important part of the home-buying process. They help buyers establish an expectation of what they can afford and often lock in a particular interest rate. Nevertheless, pre-approvals do not guarantee a buyer mortgage approval and in some cases overestimate what a person can afford to pay. In addition, some approvals are granted with obscure and hard to understand conditions, allowing lenders to later withdraw funding. This can cause serious frustration to a consumer when they wish to purchase a home, only to discover that their expected mortgage approval is not in line with what they are ultimately approved for or what they can comfortably afford.

Currently, the term pre-approval is applied to an assorted variety of agreements and the nature and conditions attached are not always communicated adequately to consumers. Some FRFIs even advertise their pre-approvals as a way to determine exactly what a consumer can afford. Members of CREA from

across the country have flagged this issue as a serious concern. It negatively impacts both buyers and sellers when sales fall through as a result of confusion.

CREA believes FRFIs play an important role in mitigating confusion and helping protect buyers from the emotional toll of an unsuccessful transaction. To protect potential home buyers, CREA recommends that the Consumer Code compel FRFIs to provide greater explanation of the pre-approval in advance of executing one and provide in writing a standard document to be signed by the borrower at the time of pre-approval. This document should clearly lay out the conditions of the borrower's pre-approval, including information on whether a credit check has been performed, that pre-approval is not a guarantee of loan approval, unless the FRFI is prepared to do so, that the pre-approval amount may not reflect exactly what the consumer can afford and what factors impact the final mortgage approval. Importantly, FRFIs should not be in a position of advertising they can determine what a consumer can afford. This is a decision a consumer must make after taking into account all relevant lifestyle variables. Finally, lenders should only be allowed to label full approvals, without conditions, as approvals. Conditional approvals should be titled as such with a clear explanation of the conditions.

Recommendation #2 – Mortgage pre-payment penalty provisions must be more accessible before a consumer signs a mortgage contract. Specifically, general conditions must be displayed prominently on a public website. In addition, prepayment provisions of a mortgage should be proactively disclosed at the time of pre-approval and, when signing a mortgage contract, if any provisions are different than what was previously presented these differences should be brought to the consumer's attention. These disclosures should not be merely upon request.

Rationale:

The introduction of the *Code of Conduct for Federally Regulated Institutions: Mortgage Prepayment Information*, took an important step forward in setting out a framework to provide consumers with more information about mortgage pre-payment penalties. CREA believes the current round of consultations on a comprehensive Code is an ideal opportunity to improve on the work already done.

While the Code encourages FRFIs to enhance borrower awareness before a consumer signs a mortgage contract, the Code allows FRFIs to make this information available on a website and upon request in a lender's place of business. Consumers may not receive the information if it is only placed on a website or available upon request.

Instead, to truly protect consumers, proactive and clear disclosure of the information contained in Section 3: Enhancing Borrower Awareness of the *Code of Conduct for Federally Regulated Institutions: Mortgage Prepayment Information* needs to be mandatory at a number of consumer touch points before they sign a mortgage contract. This includes at the time of mortgage pre-approval, prominently on a lender's website and before a consumer signs a mortgage contract.

Should any of an FRFI's prepayment provisions change from mortgage pre-approval to when the mortgage contract is signed, the consumer should be pro-actively notified by the FRFI of these changes.

To reiterate, FRFIs **must** make this information easily available and present it directly to the borrower before they sign a mortgage contract. This is important because, beyond disclosure, borrowers are afforded little protection from mortgage pre-payment penalties which are costly, complicated to calculate and lack standardization.

Recommendation #3 – Use of plain language that is not misleading, as per the FCAC guidelines, should be mandatory on all FRFIs disclosures and be accompanied by examples to illustrate conditions.

Rationale:

According to the FCAC, ‘plain language’ consists of clear and simple writing that focuses on the needs of the reader and presents information in a logical order using familiar, everyday words and expressions. It avoids jargon and uses a minimum of technical language in a manner that is not misleading, but that an audience can understand quickly and easily. Plain language knows its audience, makes material understandable, and may use visual presentation to enhance text.

With so much information presented to consumers of financial products, REALTORS® see on a daily basis the importance of documentation that can be easily understood by consumers. This recommendation is of particular importance to protect seniors and vulnerable Canadians. As the Consultation paper points out these populations “can be susceptible to financial fraud, mis-selling and poor financial outcomes due to limited capacity, knowledge or education when making financial decisions.” This recommendation seeks to provide greater understanding of financial products.

Some existing regulations and Codes already stipulate the need for clear language that is not misleading. For example, FRFIs are required to offer complaint mechanisms in plain language, and the non-binding *Code of Conduct for Federally Regulated Institutions: Mortgage Prepayment Information* has requirements that equally indicate the need for plain and not misleading language. CREA believes a Comprehensive Consumer Code should follow suit and require lenders to provide information about all financial products in language that clear, simple and not misleading.

In addition, easy-to-understand examples should be provided by FRFIs to illustrate elements of financial products covered by the Comprehensive Consumer Code. As stated in a joint paper by CREA and The Canadian Bankers Association in 2000, “the best way to communicate information is to explain it and then given an example to show how it works in practice.” For example, the costs of paying off a mortgage debt early, before the mortgage maturity date, should be laid out for the readers in a step-by-step formula they can use; and then an example illustrating a ‘typical situation’ should be given. This process should also be used to illustrate to borrowers the division of their mortgage payment between principal and interest.

Mandatory implementation of this practice, and evaluation by the FCAC, is necessary to establish best practices across institutions to the benefit of consumers. Having best practices in place will improve consumers’ understanding of often complicated information and, allow consumers to compare their

options across institutions. Ultimately, this will place consumers in a better position to make more informed selections of FRFIs and choose the FRFI and financial products that best meet their needs.

Recommendation #4 – *Make the Consumer Code mandatory and strengthen the FCAC monitoring, reporting and sanctioning powers.*

Rationale:

To achieve the desired effect of the preceding recommendations, it is vital the Consumer Code be mandatory for all FRFIs and enforceable. CREA believes that to protect consumers, universal adoption and mandatory adherence to the Code is necessary. Further to this, to achieve compliance and promote best practices, the FCAC should have the power to monitor and thoroughly report on compliance with the Code. This reporting should be easily accessible on the FCAC's website and be laid out in plain language. It should both highlight praise worthy performance and initiatives where certain FRFIs are leading the way, as well as disclose areas for improvement. A visible and transparent system which includes both praise and reprimand will be most effective at promoting compliance.

We welcome the opportunity to discuss our comments with you further. Please do not hesitate to contact Anna Laurence from my External Relations team (alaurence@crea.ca) to arrange a meeting.

Regards,

A handwritten signature in black ink, reading "Randall McCauley". The signature is written in a cursive, flowing style.

Randall McCauley

Vice-President Government and Public Relations