Umbrella Mortgages: the Pros and Cons of the Hypothecary Loan Contract

RESEARCH REPORT

Report produced by Option consommateurs
presented to Industry Canada's Office of Consumer Affairs
May 2012

Option consommateurs

Mission

Option consommateurs is a not-for-profit association whose mission is to defend the rights and interests of consumers and to ensure that they are respected.

History

Option consommateurs has been in existence since 1983, when it arose from the Associations coopératives d'économie familial movement, more specifically, the Montreal ACEF. In 1999 it joined forces with the Association des consommateurs du Québec (ACQ), which had already pursued a similar mission for over 50 years.

Principal activities

Options consommateurs has a team of some 30 employees working in five departments: Budgeting, Energy Efficiency, Legal Affairs, Press Room, and Research and Representation. Over the years, Option consommateurs has developed special expertise in the areas of financial services, health, agrifood, energy, travel, access to justice, trade practices, indebtedness, and the protection of privacy. The organization has conducted several major investigations including one on deceptive marketing practices in the retail furniture sector and another showing that despite currency parity, Canadians paid more than Americans for the same products. Every year, we reach 7,000–10,000 consumers directly, conduct numerous interviews in the media, participate in working groups, sit on boards of directors, carry out large-scale projects with key partners, and produce research reports, policy papers and buyers' guides, including the annual *Toy Guide* in *Protégez-vou*s magazine

Membership

In its quest to bring about change, Option consommateurs is active on many fronts: conducting research, organizing class action suits, and applying pressure on companies and government authorities. You can help us do more for you by becoming a member of Option consommateurs at www.option-consommateurs.org.

SUMMARY

Since 1994, under Article 2797 of the *Civil Code of Québec*, mortgage agreements have increasingly stipulated that the mortgage will be used not only as security for the mortgage loan itself, but also the present and future obligations of the consumer and sometimes those of a third party, such as a spouse. This is called a hypothecary loan contract, (or deed of hypothec) loosely referred to as an umbrella mortgage. This type of mortgage does not automatically terminate when the mortgage loan is paid off, because the mortgage stands as security against the borrower's future obligations. Obtaining additional loans is conditional on repaying part of the mortgage, or an increase in the value of the property. To qualify, the consumer must make an application to the lender and satisfy the latter that he fulfils the requirements.

There are many questions raised by this new kind of mortgage agreement. What are its advantages and disadvantages for consumers? Does it allow consumers to save on interest charges? What is the difference between the umbrella mortgage agreement and the traditional mortgage agreement?

The industry claims that the newer product has several advantages. It facilitates access to credit and helps consumers avoid paying legal fees. In fact, this type of contract allows the borrower to take out additional loans without using the services of a notary, since the contract stipulates that the mortgage stands as security against all the borrower's present and future obligations toward the lender. Some lenders, such as the Laurentian Bank, still offer the possibility of a traditional mortgage while others, including the National Bank, no longer offer that option.

In fact, the lenders we talked to said that the traditional mortgage is not currently used as security against consumer debts, except in the case of bad debts.

The experts we talked to told a different story. For example, according to Marc Boudreault, a retired professor of the University of Ottawa's Faculty of Law, the provisions of umbrella mortgage agreements are unclear, and consumers are often unaware of the extent of their liability. They only discover this during their visit to the notary, when it is too late to negotiate with their financial institution. Moreover, in the case of a joint loan, the mortgage may serve as security against all the current and future debts of another person without the co-borrower even being notified that any new borrowing has occurred. In addition, in the event that the home is sold, in order to be discharged, the consumer could be required to pay off not only the mortgage loan, but all loans secured by the umbrella mortgage, including the debts incurred by his or her spouse. This type of loan could also lead to over-indebtedness.

L'Office de la protection du consommateurs is concerned about this issue, especially about the fact consumers might subscribe to such an agreement without their knowledge.

To get a better idea of the problem, we conducted 20 semi-structured interviews with consumers who have taken out a mortgage in the past 12 months. We found that most were unfamiliar with the specific details of their credit instrument. For example, of the 13 people who seemed to have a hypothecary loan contract, only three stated that the

contract might cover other loans. It looks as if the consumers we surveyed were not paying attention to the details of their contracts.

To investigate the issue in greater depth, we conducted four focus groups, two in Montreal and two in Quebec City. Overall, participants were unfamiliar with their mortgage product, although some considered themselves to be well informed on the matter. During the focus groups, we distributed a fact sheet explaining the hypothecary loan contract and what differentiates it from a traditional mortgage. After an informal explanation of the concept, some began to wonder whether this was the type of mortgage they had. Many felt they had a traditional mortgage, even though the text they read almost perfectly matched the description they themselves had given earlier in the session, when they were asked to explain the type of mortgage they had agreed to. Despite these gaps in information, the participants in the focus groups reported that they were not in favour of legislative intervention. They did express the view, however, that consumers should be more on their guard. The participants stated that if they had the choice, they would not opt for an umbrella mortgage.

We then proceeded to identify the laws regulating umbrella mortgage agreements in Canada and to analyze the legal framework of these laws, first in Québec, then in Ontario, British Columbia and Newfoundland-Labrador. This exercise permitted us to understand the extent of the legal obligations specified in the mortgage in accordance with the broad principles of the *Civil Code* (Québec) and the common law (in other provinces), as well as the laws governing real estate transactions in those provinces.

Our analysis revealed that, in principle, owing to its accessory nature, the mortgage is extinguished when the principal debt no longer exists. But what about mortgages that secure present and future loans? In Québec, under Article 2797, the lender is entitled to refuse the borrower's application for discharge of the debt even if he has repaid the principal loan in full. The catch? His future obligations are still subject to the mortgage. Based on Article 2797, the lender may refuse to cancel the mortgage as long as all the borrower's other obligations toward the lender or those of a third party assimilated to the borrower have not been fully paid. The legal problems that could arise are obvious. Consumers need to be very careful in verifying the actual extent of their mortgage agreement with their financial institution. It is also quite possible that the mortgage advisors themselves are misinformed.

There is no law in Québec requiring the lender to inform the borrower of the extent of the mortgage agreement. Elsewhere, only the provinces of Newfoundland-Labrador and British Columbia appear to require the mortgage lender to disclose the extent of the obligation. The others are content to abide by the obligation to disclose the cost of borrowing and the rate as specified by the *Interest Act* and the regulations respecting the cost of borrowing in their respective legislations.

Recommendations

Given the above findings, Option consommateurs recommends that:

Consumers

Inform themselves about the type of mortgage proposed by the financial institution and that they read it carefully before signing the agreement with the notary.

Whenever possible, avoid taking out other loans from the financial institution to ensure that all their new debts are not secured by the mortgage on their home, unless that is their wish.

Financial institutions

Publish information on their websites about the present and future obligations of borrowers covered by mortgages and ensure that consumers can easily access this information.

Ensure that their employees are able to inform clients about the type of obligations involved in mortgage and provide them with the appropriate training.

Adjust the terms of each loan secured by the mortgage in accordance with this security, including interest rates on credit cards.

Simplify the terms of hypothecary loan contracts.

Grant an extinction of the mortgage once the loan principal is repaid in full.

The Government of Québec

Amend its legislation to require financial institutions to adjust the terms of each loan secured by the mortgage in accordance with this security, including interest rates on credit cards, unless the financial institutions accept to do so voluntarily.

Option consommateurs supports the position of the Chambre des notaires du Québec and requests that the Government prohibit the mortgage from extending automatically to new obligations, unless the consumer or the new owner of the property consents to their property being used to secure these new obligations.

The Government of Canada

Amend its legislation to require financial institutions to adjust the terms of each loan secured by the mortgage in accordance with this security, including interest rates on credit cards, unless the financial institutions agree to do so voluntarily.

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Option consommateurs
Head Office
50, rue Ste-Catherine Ouest, suite 440
Montréal (Québec)
H2X 3V4
Telephone: 514 598-7288
Fax: 514 598-8511

Email: info@option-consommateurs.org
Website: www.option-consommateurs.org

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1. Introduction

1.1 The context

Since the late 1990s,[1] Québec's financial institutions have offered a new type of mortgage contract, the hypothecary loan contract (or deed of hypothec), also known as an umbrella mortgage. This kind of mortgage may secure other loans contracted for the purchase of the property (home equity line of credit, renovation loan) and even debts that other people, (such as spouses) have contracted with the financial institution. The mortgage may also cover future liabilities. With this type of mortgage, the borrower is able to take out additional loans without going before a notary. This product is not the same as a traditional mortgage.

The emergence of this new type of mortgage contract raises many questions. What are the advantages and disadvantages of this formula for consumers? Does it allow them to save on interest charges? What is the difference between the umbrella mortgage agreement and the traditional mortgage agreement? What are the monetary obligations secured by the mortgage? Does the hypothecary loan contract make it easier to access credit? Would a borrower who wanted to switch mortgage lenders have to repay not only the mortgage loan, but also the other debts that come under the umbrella? Is the idea behind umbrella mortgages for banks to retain their customers, and in doing so, are they stifling competition?

In an attempt to answer these questions, we divided the research into six sections. In the first, we summarize the characteristics of the hypothecary loan contract and what differentiates it from a traditional mortgage and a home equity line of credit. In the second, we present the views of industry on the subject through interviews with the Canadian Bankers Association, the National Bank, RBC Royal Bank, the Laurentian Bank and the Desjardins Group.[2]

In the section three, we discuss the advantages and disadvantages of this formula and the effects it could have on the financial health of consumers; in so doing, we conducted interviews with experts, including Mr. Marc Boudreault, former professor of security and contract law in the Faculty of Law at the University of Ottawa, Mtre. Marc Migneault, advisor at the Office de la protection du consommateur, Ms. Julie Hauser, Media Relations Officer at the Financial Consumer Agency of Canada (FCAC) and Ms. Line Leduc, Director of Business Development at the Canada Mortgage and Housing Corporation (CMHC).[3] Their input assisted us in forming a clearer idea of the problem and enabling to take a critical look at the phenomenon.

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[1] According to the Canadian Bankers' Association, the National Bank was the first bank to offer this type of product, in 1998

[2] We also tried to talk to BMO Bank of Montreal, Scotia Bank, TD Bank and CIBC, but without success.

[3] We attempted, unsuccessfully, to arrange an interview with the Canadian Bar. the Competition Bureau and Ontario's Ministry of Consumers Services.

In section four, we present the views of consumers. To do this, we analyzed some 20 semi-structured interviews carried out in the winter of 2012 with Québec consumers who had taken out a mortgage over the past year. The exercise permitted us to see if they knew what type of mortgage product they had obtained, the information they were given, and what they understood. The interviewees were recruited by the research firm Research House.

We will also present the results obtained from four focus groups (two in Montreal and two in Québec). These focus groups were set up to find out how consumers understand hypothecary loan contracts and their terms and conditions and how these differ from traditional mortgage contracts. These focus groups were conducted by Environics.

In sections five and six, we identify the laws governing hypothecary loan contracts in Canada and proceed with a study of their legal framework, first in Québec and then in Ontario, British Columbia and Newfoundland-Labrador. The aim of this exercise was to familiarize ourselves with the extent of the consumer's legal obligations under a mortgage under the Civil Code (in Québec), under common law (in other provinces), and the legislation governing real estate transactions in these provinces.

Upon completion of this part of the research, we compiled a list of recommendations to help consumers make informed choices, inspire legislators to establish an effective regulatory framework and help financial institutions improve their practices.

1.2 Research method

To conduct this research, we carried out an extensive literature search. We were careful to use sources of information from government agencies such as the Financial Consumer Agency of Canada (FCAC), the Office de la protection du consommateur and private sector companies or financial institutions. We also consulted a variety of publications, for example, the brief by the Chamber of Notaries of Québec on *Bill 24*, an *Act mainly to combat consumer debt overload and modernize consumer credit rules*.

We also conducted interviews with major players in the industry. These were the Bankers Association of Canada, the Royal Bank, the National Bank, the Laurentian Bank and the Desjardins Group. These interviews allowed us to record their views about the hypothecary loan contract. Unfortunately, although we tried to contact certain other financial institutions on several occasions, they either did not return our calls or respond to our emails or simply refused to cooperate in the study. These were the Bank of Montreal, Scotiabank, TD Bank and CIBC.

To obtain a different perspective on the issue, we talked with various experts working within government agencies and professional bodies such as the Financial Consumer Agency of Canada, the Chambre des notaires du Québec and the Office de la protection du consommateur. We tried to arrange an interview with the Competition Bureau about hypothecary loan contracts. We wanted to know whether, in their opinion, such security instruments could stifle competition. Unfortunately, we did not receive an answer to our questions from that organization. However, the Financial Consumer Agency of Canada (FCAC) did make a statement on this subject. To get the views of another consumer organization, we contacted Ms. Marie-Hélène Legault, an economist and spokesperson for l'ACEF de l'Est de Montréal; an association with great expertise in the field of mortgages. However, Ms. Legault, who is the person in charge of courses on mortgages at the agency, had not studied this type of credit instrument.

The semi-structured interviews were conducted by Option consommateurs, but the people we interviewed were recruited by the firm Research House. The focus groups and the analysis of comments gathered during this exercise were conducted by the Environics Research Group.

The legal analysis of contracts was performed by Mtre. Geneviève Charlet, a lawyer who has also studied notarial law. Mtre. Charlet carried out extensive research on the laws governing hypothecary loan contracts in every province of Canada and carefully studied the documentation on this subject. She provided up an overview of the state of mortgage law in Québec under the Civil Code. She did the same for the laws of Ontario, British Columbia and Newfoundland-Labrador, which are governed by common law, and for the relevant legislation of each province.

Briefly, in carrying out this research, we have attempted to understand the various characteristics of hypothecary loan contracts and the advantages and disadvantages of these products for consumers, we have assessed how well consumers understand them, and we have made recommendations to key players.

2. The hypothecary loan contract: a complex product

We will begin by summarizing the main features of the hypothecary loan contract and the "traditional" mortgage agreement.[4] The latter is the product we are most familiar with. The consumer takes out a loan and signs a mortgage agreement on his home to secure repayment. The mortgage agreement specifies the amount and the terms and conditions of the loan and the mortgage is set at an equivalent amount. This mortgage cannot be put up as security against other loans (car loans, personal loans, lines of credit, etc.). It ends when the mortgage is paid off.

Since 1994, under section 2797 of the *Civil Code of Québec*, mortgage agreements have increasingly stipulated that the mortgage will be used to ensure not only the mortgage loan but also the present and future obligations of the consumer and, sometimes, those of third parties, such as spouses.[5] This type of mortgage may not end when the mortgage is paid because it also stands as security for the buyer's future obligations. Additional loans can be obtained if part of the mortgage is repaid, or if the value of the property increases. The consumer must apply to the lender and qualify for the loan.

According to the Association professionnelle des notaires du Québec (APNQ), this type of contract allows the borrower to contract additional loans without going before a notary, since the contract generally specifies that the mortgage will secure all the borrower's, debts— both present and future— to the lender.[6] This type of mortgage can be thought of as "umbrella" that covers all the borrower's debts against the lender who granted the mortgage.

For example, a consumer borrows $300,000 to buy a house and the lender grants the loan at a rate of 3.5%. The contract stipulates a mortgage of $400,000 at an interest rate of 20%, just to cover the borrower's other current and future debts to the lender. The following year, the borrower requests a loan of $10,000 for renovations. [TRANSLATION] "The mortgage consented at the time of acquisition of the house could, in the wording of the contract that the consumer has signed, automatically guarantee that loan to the same lender without having to sign a new mortgage contract," the APNQ states[7]. More specifically, the borrower's new debts and, if applicable, those of his spouse, may automatically be secured by the mortgage on their home. The practices and the extent of the debts whose repayment is secured by the mortgage may vary from one institution to another. It is possible that different interest rates could apply to loans grouped under the "umbrella."

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[4] We will return to this point in greater detail in section 5, which presents the legal analyses of these contracts.

[5] Source: *Mémoire de la Chambre des notaires du Québec sur le Projet de loi 24 intitulé Loi visant principalement à lutter contre le surendettement des consommateurs et à moderniser les règles relatives au crédit à la consommation,* Chambre des notaires du Québec, November 2011, p. 15.

[6] *Lumière sur le financement hypothécaire*, Option consommateurs et Association professionnelle des notaires du Québec, 2010.

[7] Ibid.

To learn more about how financial institutions inform their clients about hypothecary loan contracts, we have conducted a search of their websites.[8] This research did not uncover any information specifically related to the present and future obligations of the borrower covered by the mortgages or the extent of the latter's commitment to the financial institution.[9]

We recommend that financial institutions publish information on their websites about the present and future obligations of borrowers covered by mortgages and ensure that consumers can easily access this information.

[8] See Appendix A

[9] This research was carried out during the summer of 2011. It is possible that certain points of information escaped the researcher's notice because they were not emphasized. It is also possible that this information was missing.

3. The lenders' point of view

We asked financial institutions and the Canadian Bankers Association (CBA) to give us their views on hypothecary loan contracts and to present the advantages and disadvantages of the formula. The CBA, the Royal Bank, the National Bank, the Laurentian Bank and the Desjardins Group agreed to answer our questions. To avoid repetition, we present only the significant parts of these interviews. We will first give the views of the CBA, then those of the other players in cases when certain items are different or when information was provided that was not contained in the first interview. Readers can assume that, except where specified, the statements by the other banks were similar to those made by the spokesperson for the CBA.

3.1 Canadian Bankers Association

In the opinion of Randy Hopkins, Consumer Relations Advisor at the Canadian Bankers Association (CBA), the hypothecary loan contract was introduced into the market in response to consumer needs. "According to our statistics and those of the Canadian Association of Accredited Mortgage Professionals, 80% of borrowers who want to refinance or renew their mortgages stay with the same lender. Many of them have to take out a second mortgage and pay additional fees when they want to refinance their home or access its net worth. The hypothecary loan contract was set up to give homeowners access to credit without having to pay legal fees or registration costs."

Since the mortgage can be used to secure other loans from the same financial institution, can consumers benefit from a lower interest rate, such as the interest they pay on their mortgage? "The rate of the loan for purchasing the home may be different from that for a line of credit, for example, but both types of loans are offered at market rates," Hopkins says. "Also, you can have different interest rates for the various loans covered by the 'umbrella' mortgage. Each loan has its own rules, rates, terms, conditions, and so forth." *Does the consumer who wants to sell his home or change financial institutions have to repay all the loans under the 'umbrella mortgage'?* "In principle yes, he may have to," he said. "In most cases, if a consumer changes to a financial institution that offers similar products, he will arrange to borrow a sum from the other lender that will enable him to repay the balance of his mortgage loan and his other loans."

Many people purchase their homes jointly with their spouses. What could happen in the event of separation or divorce? Could one spouse be held liable for loans taken out by the other? " Both parties are responsible, just as they would be if they had both signed a traditional joint loan contract. The same rule applies to all joint loans. As long as both names appear in the contract, each remains responsible. "

Can consumers still get a classic mortgage? "Unfortunately, we have no statistics on this, but we do know that the umbrella mortgage market is growing," he adds. "However, those who do not want this type of instrument still have access to other formulas. The traditional mortgage has not disappeared. Financial institutions offer both classic mortgages and umbrella mortgages. There's great choice in the market."

As we can see, the umbrella mortgage may be an interesting credit instrument, but is a complex product, nonetheless. Consequently, it is important that consumers who opt for this product do so knowingly. In Québec, it is the responsibility of the notary to educate consumers about the extent of their legal obligations; elsewhere in Canada, this task sometimes falls to the financial institutions (we shall return to this point later). In any case, at that stage, it is too late for consumers to change their minds. So we asked Mr. Hopkins if he believed the information disclosed by the financial institution allows the consumer to make an informed choice. “Certainly,” the CBA spokesman replied, “The information about the terms, conditions and rates is set out in the mortgage documents. And the advisors make sure that the clients have read and understood the documents before they sign them. So the information is there, and the banks are making an effort to encourage clients to read it. But, ultimately, it’s the clients’ responsibility to ensure they understand the commitments they are making.”

Finally, can the consumer go back if he doesn’t realize what kind of contract he is about to sign until he sees the notary? “It would be better if the consumer understood the characteristics of the product before going to the notary,” the CBA spokesman said, “(..) but if this were not the case, a simple telephone conversation with the bank might be enough to fix the situation. The consumer may not have to return to the financial institution and start the whole approval process over again.”

3.2 The Royal Bank of Canada

In its written response to our request, the Royal Bank of Canada maintained that this formula allows consumers to save on interest costs: “In most cases, the loan is backed by the equity in the property, which allows the borrower to benefit from lower interest rates.” According to the RBC, the formula has definite advantages, particularly as regards interest rates, terms and conditions of repayment, and greater flexibility in using the funds made available. *Would a borrower who wanted to change from the RBC to another mortgage lender have to repay not just the mortgage loan but all the other debts covered by the umbrella?* “There are no absolute rules in this regard. It all depends on the circumstances of each client. “

3.3 The National Bank

Eric Meunier, the spokesman for the National Bank, said that the hypothecary loan contract was originally developed to permit clients to finance additional home-related loans such as renovations. “The rate is determined on the basis of the current mortgage rate on the market,” he says. “For people who practice good debt management, this is probably one of the least expensive modes of financing, provided you amortize the loan over a shorter period than the useful life of the product you want to finance. “*Do real estate mortgage loans secure the client’s past and future debts?* “The hypothecary loan contract could, for example, cover a debt on a credit card that was incurred after the mortgage agreement, but in fact there is no relation. For example, if you decide to change financial institutions if your mortgage expires, you don’t have to cancel your credit card to pay off your mortgage, unless you are in default and you have a bad credit rating.”

He said that the advisor at the bank explains the characteristics of the loan to the client, including a brief statement that he will have to agree to a real estate mortgage and what this entails. “The client will obtain more detailed information about the legal consequences of the mortgage from the notary, since the latter is obliged to explain each clause of the mortgage to clients, including their present and future obligations secured by the mortgage,” he added. A client who wants to opt for a traditional mortgage should go to another lender. “The National Bank does not offer a traditional mortgage. In fact, very few banks still do,” he added.

3.4 The Laurentian Bank

Laurentian Bank customers have a choice between a hypothecary loan contract as part of an “Owner’s Kit” and a traditional mortgage. “If the client does not want the ‘Owner’s Kit,’ we will ask the notary to apply the mortgage to just on the amount of the loan,” says Eric Chamelot, Assistant Vice President, Product Management at Laurentian Bank Financing. “In that case, it’s the same as a conventional mortgage.” What is more, the Laurentian Bank does not create mortgages for amounts higher than that of the secured obligation. “Some lenders go much further than us and base the amount on the increased value of the property,” Mr. Chamelot said. He added, “At present, your credit card contract and your mortgage contract are unrelated. We will not require you to pay off your credit card to liberate you from the mortgage.” Mr. Chamelot acknowledged that this rule might change.

3.5 The Desjardins Group

According to Mr. Nicolas Fréchette, principal advisor, mortgage financing with the Desjardins Group, this type of contract offers the possibility of agreeing to a higher limit than the mortgage loan. "On the other hand, it does not cover other products such as consumer loans. However, if you have paid off part of your mortgage, you may be able to consolidate your debts. Using this tool, you could benefit from the mortgage rate or a blended rate, depending on whether you are renewing your mortgage or not.”

Option consommateurs recommends that financial institutions ensure that their employees adequately inform consumers about the types of obligations that are secured by the real estate mortgage.

Option consommateurs recommends that financial institutions supply consumers with a plain language brochure that explains the extent of the obligations secured by the real estate mortgage.

Option consommateurs recommends that financial institutions continue to offer the "traditional" mortgage.

4. The stakeholders' point of view

4.1 La Chambre des notaires du Québec

While this formula may seem attractive, it also has many disadvantages for consumers, according to Mr. Marc Boudreault, a retired professor of the Faculty of Law at the University of Ottawa and spokesperson for the Chambre des notaires on the issue of hypothecary loan contracts.[10] [11]" The clauses of hypothecary loan contracts are ambiguous and unclear. It is extremely difficult, even for an experienced lawyer, to determine what the obligations secured by the mortgage are. For example, there are 52 pages in the Bank of Montreal contract. When you try to understand one clause, it refers you to another five. Also, at the financial institution itself, consumers are handled by employees who are not always trained to inform them adequately. Often too, consumers will do business with a mortgage broker to obtain a loan. However, the broker primarily sells an interest rate."

The result? Consumers are often unaware of the extent of their liability. They learn they are about to sign such a contract only once they are at the notary. "Unfortunately, at that point, it is too late to negotiate with their financial institution," Mr. Boudreault said. "Consumers should know the details of their hypothecary loan contract before they leave the financial institution. If the need arises, they can negotiate or change to another financial institution. "Right now," adds Sylvie Janelle, president of l'Association professionnelle des notaires du Québec, "all the consumer can do is to avoid taking out other loans from that financial institution in the future."

This is not the only difficulty consumers are likely to encounter. If a consumer purchases a mortgage jointly with another person, e.g. a spouse, it is possible that the mortgage will secure all the spouse's current and future debts, even without the former being notified of any new borrowing. "For example," Boudreault says, "in order to sell the house, the consumer could be required to pay off not only the mortgage but also the spouse's line of credit before the mortgage can be extinguished."

In its brief, the Chambre des notaries du Québec also stresses the following:

> [TRANSLATION] Over time, the mortgage has become a contract of adhesion, and we have observed that several lenders use their power to draft the contract however they please, by inserting a stipulation in the contract that the mortgage will also automatically secure any future obligation that the debtor or a third party, such as a spouse, may contract against the mortgagee. The CNQ believes that in the case of consumers, it should be prohibited for the mortgage to extend automatically to new

[10] Marc Boudreault is a former professor of security and contract law in the Faculty of Law at the University of Ottawa. In 2007, he was involved in setting up the Master's program in notarial law, which, in addition to training future notaries, supports research and reflection in this specific field of law.

[11] Following are some extracts of this interview. For more complete details, refer to section 5 of this report.

obligations, without the consumer or the new owner of the property consenting to his property being used to secure these new obligations.[12]

4.1.1 Over-indebtedness

According to Mr. Boudreault, the hypothecary loan contract sometimes provides that the mortgage be set higher than the value of the home. “The lending institutions hope that the borrower’s future obligations will be secured by the mortgage up to the fixed amount in the event that the value of the home goes up.”

“By acting in this way, lending institutions could contribute to consumer indebtedness. Currently, according to the Bank of Canada Review,[13] the ratio of Canadian household debt to disposable income is around 150%, compared to 110% in 1999. This is unheard of. A decline in the housing market could cause the market to collapse due to the interrelatedness of consumer credit and mortgage lending.” In its brief, incidentally, the Chambre des notaires makes the point that in any law dedicated to controlling excessive debt[14] [TRANSLATION] “it is of fundamental importance to find measures that target both consumer credit and mortgage lending.”[15] As evidence, the Chambre cites the most recent financial crisis in the United States.

4.1.2 Losing your home

Under the real estate mortgage contract, the creditor is protected wall to wall. “While it’s important not to generalize,” Boudreault says, “anyone who fails to pay back their loan under this ‘umbrella“ could very well lose their home. That is why the interest rate on loans secured under the mortgage should be set according to the security given to creditors. Such a measure would prevent the balance of a credit card secured by a real estate mortgage having an interest rate of 20%.”

4.2 L’Office de la protection du consommateur

Marc Migneault, a lawyer in the Office de la protection du consommateur, had a few reservations of his own: “Our reading of the jurisprudence has not convinced us that the lending institutions are entitled to use the mortgage to repay other debts covered by the umbrella, except in cases of default.” We should mention here that within the current legislative framework, first mortgages are almost totally exempt from the application of the *Consumer Protection Act*.[16]

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[12] *Mémoire de la Chambre des notaires du Québec sur le Projet de loi 24 intitulé Loi visant principalement à lutter contre le surendettement des consommateurs et à moderniser les règles relatives au crédit à la consommation*, Chambre des notaires du Québec, November 2011, p. 16.

[13] The report is entitled, *“*Situation financière des ménages et stabilité financière.*”* Source : http://argent.canoe.ca/lca/affaires/canada/archives/2012/02/20120223-113400.html. consulted in March 2012.

[14] *Bill 24, An Act mainly to combat consumer debt overload and modernize consumer credit rules*, was at the committee stage when this report was being prepared.

[15] Ibid. p.17

[16] See Section 5.

Could setting the mortgage at a higher value than that of the home force consumers into debt? In his view, imposing a maximum level of debt is a very delicate matter. “For example, the parents of a gravely ill child whose only treatment is in Europe would take a very dim view of being deprived of the right to borrow more than a certain amount,” he said. “It's the same for the owner of an ancestral home that will be worth double once it is renovated. There are risks in doing things this way, but also advantages. Furthermore, if it were not allowed, consumers would have to use the services of a notary to obtain further loans secured by their real estate mortgage. And in that case, there would be fees to pay.”

Migneault nevertheless believes that the scope of the real estate mortgage is too wide and that this is a source of concern. “The Office de la protection du consommateur is mostly concerned about the fact that consumers could subscribe to such a contract, without realizing it. Once at the notary, the consumer is not receptive to such information. A mortgage that can secure present and future debts might seem like a very abstract affair. Are consumers likely to halt the transaction and thereby expose themselves to significant penalties? “

4.3 The Financial Consumer Agency of Canada

The Financial Consumer Agency of Canada (FCAC), has a number of tips for consumers. According to the organization, an umbrella mortgage may allow the consumer to save on interest charges. “Everything depends on the terms of the contract between the consumer and the lender, including the interest rate on the initial loan and the interest rates that will apply to any loans that the consumer takes out in the future. First of all, this involves comparing the interest rate that the consumer who wants to borrow an additional amount would have access to through the umbrella mortgage to the rate that he could get from another lender, Second, it involves considering whether he already has loans that he wants to transfer to an umbrella mortgage, and if so, how much it would cost to terminate the loan agreements.”[17]

4.3.1 A captive clientele?

Under the terms of an umbrella mortgage contract, the lender usually requires that all the debts under the umbrella be paid off if the consumer wishes to transfer his mortgage to another lender. This could discourage a consumer from switching financial institutions. “So it’s important for the consumer to check what obligations would apply in this situation and consider them before making a decision,” the FCAC says.

Does this credit instrument help financial institutions retain customers? The FCAC considers that it could encourage customers to consolidate all their credit needs with the same creditor if the latter offers benefits that they consider important. “If a customer had to repay all the loans under the umbrella before transferring any or all of his loans to another lender, it could make changing lenders more difficult, depending on the

[17] Julie Hauser, media relations officer at ACFC, answered our questions in writing.

customer and how much support the new lender provides in the transition process. Seen from that perspective, the umbrella mortgage could help build customer loyalty. "

By acting in this way, are lending institutions stifling competition? The FCAC's opinion is that consumers have many options in the mortgage market. "As with any other product, if they are to benefit from the competition and choose the mortgage best suited to their situation, it is important for consumers to do research, shop around and consider the pros, cons and obligations of each option before making a choice, " the agency says.

4.4 Canada Mortgage and Housing Corporation

According to Line Leduc, Director of Business Development at CMHC, this type of loan is called a collateral mortgage. "It's an alternative to a traditional loan. The borrower ends up with two documents: a mortgage agreement and a collateral mortgage contract. If there is a section of the loan that is not amortized, for example, a line of credit, the risk will be totally assumed by the lender, and is not insured by CMHC. "

Option consommateurs recommends that financial institutions simplify the terms and conditions of hypothecary loan contracts.

Option consommateurs recommends that financial institutions ensure that their employees are able to inform consumers about the types of obligations attached to the mortgage and provide them with appropriate training.

Option consommateurs recommends that financial institutions grant extinction of the mortgage once the principal loan is repaid in full.

Option consommateurs recommends that the Government of Québec and the federal government amend their respective legislations to require financial institutions to adjust the terms of each loan secured by the mortgage in accordance with the terms of this security, including interest rates on credit cards, unless the financial institutions agree to do so voluntarily.

Option consommateurs supports the position of the Chambre des notaires du Québec and requests that the government prohibit mortgages being extended automatically to new obligations unless the consumer or the new owner of the property consents to their property being used to secure these new obligations.

5. The consumers' point of view

5.1 Semi-directed interviews: highlights

In parallel with our study of the current laws, we conducted semi-structured interviews with 20 consumers. This exercise allowed us to amass a considerable amount of data on how consumers perceive the hypothecary loan contract, what they think differentiates it from traditional mortgage loans, and the information they obtained in this regard.[18] The consumers we interviewed had all taken out a mortgage in the past twelve months.

Before proceeding with this exercise, we first developed an interview grid to help us learn more about the consumers' experience with mortgages.[19] We also made sure we could find the clause stipulating that the real estate mortgage covers the future obligations of the borrower, aided by a document prepared by notary François Lebreux,[20] a copy of which we obtained at the round table to reform the *Consumer Protection Act*. The aim was to help consumers identify the clause, if one existed.

Prior to the interview, the participants were instructed to read their mortgage contract. They also had to have it at hand to consult during the interview. This was not always possible. Some talked to us while they were at work, and had not brought their notarized contract with them. Others confused the notarized contract with the loan agreement. Still others were not able to get their hands on the notarized contract.

Profiles of interviewees

The semi-structured interviews were conducted in February and March 2012. The participants lived in Québec in the Greater Montreal metropolitan area and vicinity. We interviewed 20 people, 13 women and 7 men. Of these, 19 worked full time and 1 was retired, 7 were single and 13 were married. They were from 25 to 63 years of age.

Of those surveyed, 12 had taken out a mortgage in the last 12 months, 7 within 6 months and 1 in the last 3 months. Of these, 4 had done business with the Desjardins Group, 3 with National Bank, 3 with TD Bank, 3 with Scotiabank, 5 with RBC Royal Bank, 1 with Manulife and 1 with BMO Bank of Montreal. A little over half were new to mortgages. Thus, this was the first mortgage for 14 people, the second for 2, and the third for 3 or more (one participant did not seem to know how many she had had.)

During this telephone conversation, we specifically asked participants if their mortgage advisor had offered different formulas when they were applying for a mortgage. In most cases (17), they said their mortgage advisor had gone over the basic concepts (mortgage

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[18] The semi-directed interviews took place in February and March 2012.
[19] See the list of questions in Appendix B.
[20] This document was obtained during a round table on the reform of the *Consumer Protection Act*, organized by the Centre d'études en droit économique (CÉDÉ) at Laval University in January 2012. Mtre. Dominique Gervais, legal advisor in Option consommateurs' legal department, took part in that event.

insurance, variable rate and fixed rate mortgage terms, lines of credit, credit cards, payment terms, etc.).

5.1.1 Could they understand the document?

We next asked the participants why they had opted for a hypothecary loan contract, rather than a traditional mortgage. The result was that 18 out of 20 people did not understand the question and thought they had a traditional mortgage. However, 14 people had signed a document at their bank and had read all or some of it prior to signing. Two people stated that they had not signed any document at their bank. Only the person who had done business with Manulife was familiar with the hypothecary loan contract and had chosen it purposely. One National Bank customer knew his real estate mortgage covered other borrowing, including lines of credit. He made the comment that this formula gives him peace of mind if something goes wrong, but he did not want the mortgage on his house to be linked to his line of credit when he was ready to pay off the loan.

We then we asked whether participants had been surprised by certain details when they read the document. A TD Bank customer said he was surprised by the interest he would have to pay. A Desjardins Group customer reported being surprised by the charges, while a National Bank customer said he was not very comfortable with technical terms. The other participants said they were well informed. One, a National Bank customer, even said he was quite unconcerned. “I‘m a long-time customer,” he said. Another participant said he was informed quite partially. “There were 20 pages in my contract,” he said. “Often it’s not even the person in front of you who approves the loan. He or she collects information in a computerized file that has to be approved by a third party. I'm not even sure that person is completely familiar with all the terms.”

5.1.2 Other loans

Were the participants looking for money to pay off debts (credit cards, car loans, etc.) when they took out their mortgages? One of them would have liked to do that, but did not request it, and 19 said they did not want that option. Would you have liked to have money for future projects (renovation, line of credit, etc.)? The majority of participants said they did not wish to take advantage of this option, while six opted for a line of credit.

We also asked them if the product they were offered covered other loans. The majority of participants stated that their product did not cover other loans. One, however, said he would have access to his line of credit as he paid off the mortgage, another said he was free to use the credit however he liked, while another said the option provided easier access to credit. Were the participants well informed about the pros and cons of such a formula? When we asked this question, most participants did not differentiate between a traditional mortgage and a hypothecary loan contract. They were unable to answer the question. Among those who knew what it was, one person was concerned that the formula might push him into debt.

5.1.3 At the notary

We then turned our attention to how the transaction was concluded at the notary. Of those surveyed, most had no surprises at the notary. One said she could not remember any details except that she was anxious for the transaction to be completed; two others told us that the lawyer had explained the advantages and disadvantages of the hypothecary loan contract. “He told us that the mortgage could cover other loans, and that was something that scared us,” one participant said.

5.1.4 Present and future obligations

We then asked respondents whether their contract included a clause on present and future obligations and to read it to us. This exercise was not always successful. Sometimes, consumers were able to identify the clause, sometimes not. However, 3 participants said they had found such a clause and 10 read it to us. When participants were unable to identify the clause, we explained what it was about. Next, we asked the respondents what they thought. The majority felt that it had the advantage that they could save on notarial fees. “It may be a good thing if there is work we need to do,” one participant said. “Consumers will benefit from a better rate than if they use their credit cards.” “I don’t think it’s the best solution, but it provides us with a cushion in an emergency,” someone else said. “However, I want my house to be one hundred per cent mine when I finish paying off my mortgage.” “It's a good formula for home-related expenses,” another said.

We then asked about the disadvantages of such a formula. Some stated that their mortgage should not cover consumer debts such as credit cards. Others said that this formula posed no inconvenience because they had no intention of getting deeply into debt and would make sure they met their financial obligations. One person, however, said it could lead someone into debt and ultimately lose their home.

Two participants agreed to send us their notarized contracts. These loans were contracted with the Bank of Montreal and the National Bank respectively, and the contract contained a clause stipulating that the mortgage covered the debtor’s future obligations. The Bank of Montreal customer was not aware of this clause and the extent of his obligations secured by the real estate mortgage and, during our telephone conversation, was convinced he had a conventional mortgage. He did, however, know that he would have access to funds as and when he paid off his mortgage. The National Bank customer was aware of the characteristics of his contract, as he had been informed of them by both the employee at the bank and the notary.

Finally, we wanted to make some correlations. Of the 13 people who appeared to have an umbrella mortgage, only three knew that it might cover other debts and that they had learned this from their mortgage advisor. “He even increased the amount of my mortgage in my presence,” one participant said. In some cases, participants did not seem to make a connection between the “the present and future obligations” clause and the possibility of obtaining other loans covered by the real estate mortgage.

There are several possible explanations for this phenomenon. Buying a home is a major investment and can be a source of significant stress, so it is possible that the participants were not paying attention to the details of the contract. Often, according to the experts we interviewed, consumers will be interested primarily in interest rates and will not bother about other items that may nonetheless have an impact on their personal finances. Also, in Québec, the law does not require the mortgage lender to explain the extent of the mortgage burden. Finally, the time elapsed since the loan is another likely factor; memories, by their nature, tend to fade.

5.2 The focus groups

We entrusted Environics Research Group with conducting four focus groups in February 2012 (two in Montreal and two in Quebec City) and with preparing a detailed report.[21] The participants in the Montreal group were anglophones and the participants in the three other groups were francophones. In total, we collected the opinions of 32 people.[22]

Each group consisted of eight participants, an appropriate number for this type of qualitative research[23]. The participants had to have bought a home in the last ten years. Within each group, the participants had varying levels of experience with mortgages: some had just bought their first home, while others owned several homes or had obtained mortgages on several occasions. These focus groups were designed to find out how well consumers understand the hypothecary loan contract and its related terms and conditions, and what differentiates it from the traditional mortgage agreement. We also wanted to know what they thought of the clauses relating to the hypothecary loan contracts of three financial institutions. To prevent the financial institutions from being identified, their names were blocked out.[24] The goal was not to target a particular institution, but to obtain feedback from participants on their understanding of the clauses.

5.2.1 The progress of the focus groups

At the outset, the facilitator asked the participants questions about their general experience of mortgages. He then gave them a document containing a brief definition of the traditional mortgage and the hypothecary loan contract in order to see how much they understood.[25] The facilitator then distributed the model clauses to the participants and asked them for their impressions. Finally, he asked them for their comments.

5.2.2 Analysis of results and discussion

Following are the main observations by Rick Nadeau,[26] who led the four focus groups, as well as the observations of the author of this study, who attended two focus groups held in Montreal.

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[21] See detailed report in Appendix C
[22] See the discussion guide in Appendix D
[23] See the detailed profile of participants in Appendix E
[24] These were the Desjardins Group, Industrial Alliance, and the National Bank. According to Statistique Québec, the market share of the financial institutions in the residential mortgage sector is confidential.
[25] The French and English versions of this information sheet are presented in Appendix F.
[26] The report by Environics entitled *"Focus Group Report on Deeds of Hypothec (Umbrella Mortgages)"* is presented in Appendix C

5.2.3 Personal experience

The participants in each group had to specify the most recent mortgage agreement they had signed, the circumstances in which this took place, and their experience with mortgages in general. The results were as follows: while most of the "experienced" consumers seemed to know more about the type of products they had, and some "inexperienced" consumers felt they knew their product, while many "experienced " consumers felt that they had only a vague general understanding of their product.

We also had to consider how the consumers interpreted the questions. Most participants based their responses on how much they knew about the terms of their mortgage (interest rate, amortization period, payments, term, etc.). However, those who had "shopped around" for the loan based them more on their knowledge of the market.

The moderator also asked participants what they thought of their most recent mortgage experience. The majority reported having had a positive experience. They said that the creditor's representative was attentive and able to inform them and answer their questions. When asked what items were discussed at this meeting, participants mentioned interest rates, fixed and variable interest rates, the amortization period, etc.[27]

5.2.4 The type of mortgage

Although they said they were knowledgeable about their mortgage product, no participant reported having a hypothecary loan contract. Most of the participants in the Montreal focus groups believed they had a traditional mortgage, while the participants in the Quebec City group reported having either a traditional mortgage, or a home equity line of credit. Some described the type of mortgage they had in detail, and their descriptions corresponded to the hypothecary loan contract. However, they were sure they had another type of mortgage.

There are two factors that could explain this phenomenon. The participants knew they had access to a home equity line of credit. The name of the loan used by the institutions has an impact on consumers' perception of the product they own. The best known example is the "Versatile Line of Credit" offered by Caisses Desjardins.

5.2.5 Conditions and contracts

The facilitator urged the participants to recall their contractual obligations. Most said that they remembered that the bank can seize their homes in case of default. Some also remembered that there was a penalty or fee if they decided to renegotiate or repay their mortgage before term.

All the participants recalled signing a mortgage agreement with their financial institution. In each group, only a few people reported having read the entire contract before signing it and several reported that they had glanced through it at most. Also, only a few felt that the document was "understandable," while most felt it was more or less easy to understand. Several said they needed to consult someone they knew to help them

[27] See page 3 of Appendix C for a list of these items.

understand the contract, in addition to what was explained by the creditor and the notary. For example, one young consumer said she asked her parents while others (mostly women), asked their spouses.

Many felt they understood the key clauses relating to the most important aspects of the mortgage (e.g. interest rates, amortization, payment frequency, etc.) and did not feel the need to scrutinize the other clauses of the contract to see if they might be detrimental to them.

5.2.6 The notary's role

Beside the fact that they found the fees high, most participants agreed that the role of the notary is to "legalize" the transaction and explain the contract to the client. They believe that this role is important for consumer protection. Some participants felt that their notary had not been careful enough; in fact, some do not remember the notary reading the entire mortgage contract. At the meeting, the notary had presented several documents and perhaps some details were skipped. Were they surprised at certain features of their mortgage contract when they were at the notary? None of the participants recalled having been surprised by any clause whatever in their mortgage.

5.2.7 Renegotiation, additional loans and sale of the home

Since certain clauses of the hypothecary loan contract may affect their ability to renegotiate a mortgage or to obtain additional loans or sell their home, we explored each of these factors with the participants.

<u>Renegotiation</u>. Only a few individuals had tried to renegotiate their mortgages. Apart from having to pay a penalty, these participants did not recall any issues related to renegotiation. This process may have been be simplified because the renegotiations often took place at the same institution.

<u>Additional borrowing</u>. Only a few individuals had tried to obtain further loans from the institution that issued their mortgage. This was mostly in the form of a line of credit, at a slightly higher rate than that of the mortgage. In every case, there were few formalities, just a little paperwork, and no one remembers having to contact his notary. Most of these participants understood that this new loan was secured by their home, and that, in the event that the latter was sold, they would also have to pay off the line of credit.

<u>Sale of the home</u>. Only a few individuals had tried to sell their home. As in the cases of renegotiation and additional borrowing, these participants stated that the exercise had proceeded without incident and that their financial institution had no specific requirements. There are two factors that could explain this phenomenon. None of the participants recalled having other debts or loans with the financial institution holding the mortgage. Most had taken out a new mortgage with the same financial institution.

5.2.8 The hypothecary loan contract

The participants were given a sheet explaining the hypothecary loan contract and the traditional mortgage. Prior to reading this sheet, very few participants had ever heard of hypothecary loan contracts or umbrella mortgages. Feedback from participants suggests that they were more familiar with the concept than the name by which it is known.

Once the concept was explained informally, some participants, particularly those in Quebec City, began to wonder if it was the type of mortgage they had.

Some still believed they had a traditional mortgage or a home equity line of credit, even though the text they read about the hypothecary loan contract corresponded almost exactly to the description they themselves had given earlier in the session when they were asked to explain the type of mortgage they had.

Others acknowledged that the security instrument looked like what they took to be a "home equity line of credit."

Impressions about the hypothecary loan contract. If given a choice, the participants said they would not have chosen the hypothecary loan contract. When asked them about the pros and cons of this concept, the participants in each group brought up the following points:

Advantages	Disadvantages
- easy, convenient access to funds - access to emergency funds - lower rates for additional loans, compared to a loan unsecured by the mortgage - less expensive because you do not need to contact a notary - less paperwork to get a new loan - all loans are with the same bank; it is easier to manage - by taking out all your loans with the same financial institution, you can expect more recognition from them	- too easy access to funds - borrowers stay in debt longer - the loan is linked to your mortgage if you sell your home - could encourage people to get into debt or take on more debt – becomes a "debt pit" - people do not know how the 20% rate is applied

While the list of advantages tended to be longer than the list of disadvantages, most felt that the disadvantages or risks outweighed the advantages.

5.2.9 Comparison of typical clauses

Standard clause from a traditional mortgage

The participants were asked to study a sheet containing a standard clause from a traditional mortgage and two examples of clauses from a real estate mortgage.

Financial institution A
12. Principal hypothecs
To secure the performance of its obligations under the terms of this contract, the Borrower hypothecates in favour of the Lender from this date the following properties (collectively the "Hypothecated Property") to the extent of the sum of (CDN $) with interest at the rate of twenty percent (20%) per year, the property described as follows:

Many participants understood the key premise of the clause and could explain the obligations of the borrower in their own words. They did not all clearly understand how the "20% per year" rate could be applied (because it was not the type of rate they were used to). Finally, they understood that the lender can seize the borrower's home in the event of default.

Standard clauses from hypothecary loan contracts

Next, participants were asked to read the following clauses from hypothecary loan contracts:[28]

Financial institution B
12. Hypothec
To secure the repayment of amounts present and future owed to the Caisse for the loan(s), advances or credit granted under the credit contract, as well as amounts owed due to possible increase(s) of the amount of the loans, advances or credit, and due to another loan or loans or another form or forms of credit being granted that the parties could agree to subject to the stipulations and to the hypothecs provided for hereunder, as well as the repayment of amounts that could be lent anew to the Borrower and to the eventual purchaser of the property by virtue of Section 14 "Multiproject Option," in principal, interest at the rate of fifteen percent per annum, costs and accessories (this loan or these loans and all aforementioned amounts are collectively referred to hereinafter as "the loan"), and to secure the performance of other obligations stipulated in the credit contract(s) and herein which arise from or are accessory to these obligations (all the aforementioned obligations, including those related to the repayment of the loan, are collectively referred to hereinafter as "the secured obligations"), the Grantor hypothecates in favor of the Caisse for an amount of _ ($_), the following immovable property, including any movable property, present or future, incorporated with, attached or joined to the property and considered to be immovables under the law, hereinafter referred to as the "Property," namely:

Overall, the participants' reactions were very negative. Only a few felt they understood the clause, and most found it was too long and too complex for them to make sense of it.

[28] See document B in Appendix C.

Some gave up reading. The facilitator asked the participants if this was the type of clause they would ask the notary to explain. Almost everyone said that it was.[29]

Financial institution C

HYPOTHECARY LOAN CONTRACT 14596-001 (2007-10-29)
3.1 Principal Hypothec
To secure the payment of the Indebtedness and the performance of all obligations of the Debtor hereunder and under any Credit Agreement, as well as to secure the performance of all other obligations of the Debtor to the Bank, present and future, direct and indirect, the Debtor hypothecates the following Immovable for the sum of ____ Canadian dollars ($), with interest at the rate of twenty percent (20%) per annum from the date hereof:

While participants found that the clause was simpler and easier to understand than the preceding clause, they thought it was not clear enough. In fact, they felt the two clauses represented two extremes. While the first clause was too long and complex and was extremely detailed, the second clause was not detailed enough and left room for interpretation. The participants were bothered by the following:

They did not know how to interpret the 20% rate and how it would be applied to their mortgage and future loans.

Although the majority understood what was meant by a “direct” obligation, they were unsure about “indirect” obligations. “Could that refer to loans they might take out from other banks?”

5.2.10 Unsuspected risks

Participants were asked to state whether they felt they would be exposed to more or different risks with a hypothecary loan contract than with a traditional mortgage. They argued that the risk of getting into debt is higher with a hypothecary loan contract, due to the presumed ease of access to funds. However, if borrowers are disciplined and do not use the extra credit they have access to, the risk is essentially the same. Some felt that the hypothecary loan contract gives the financial institution more flexibility with respect to seizure in the event of default. Finally, most participants believed that the risk is no greater with one product than with another, as long as borrowers understand the extent of their contractual commitment.

[29] For a full report of the participants’ reactions, see Appendix C.

5.2.11 Overall Impressions

We asked participants if the hypothecary loan contract is something they would consider. Most said they would opt for another type of credit instrument, primarily for two reasons.

When they go to a financial institution to discuss a mortgage, they want the funds to finance the purchase of their home and nothing else. They did not foresee any difficulties with a hypothecary loan contract, as long as it was used only to borrow the money to buy the home; however, they would prefer to have access only to the credit they truly need.

Several wondered how the 15% or 20% rates would be applied.

5.2.12 Better regulations?

Based on what they heard and discussed during the focus group and on their own experiences, most felt that a combination of "consumer vigilance" and standardization of clauses should be sufficient to improve regulations. The participants seemed to want government to play a minimal role in this area.

Option consommateurs advises consumers to learn about the type of mortgage contract they are about to sign and to read it carefully before signing the contract at the notary.

Option consommateurs advises consumers to avoid, as far as possible, taking out other loans from the same financial institution to ensure that all these new debts are not secured by the mortgage on their home, unless that is their wish.

6. Mortgages that secure future obligations: the legal situation in Québec

Before discussing the current legal situation with regard to mortgages (immovable hypothecs) securing future obligations, we think it important to provide an overview of the history of this new agreement. Québec civil law has undergone significant reform, a process that began in the fifties and culminated in 1991[30] with the adoption of the *Civil Code of Québec* (*CCQ*). This reform resulted in tremendous changes in the mortgage system. Henceforth, privileges, prior claims and mortgages would all be covered by Book Six of the *Code*, entitled *Prior Claims and Mortgages.*[31]

It appears that the obligations that can be secured by an immovable hypothec were also affected. The specificity principle of the mortgage has changed, and it is now possible, due to the codification of a line of authority that began in the last century, to secure present, future, identified and unidentified obligations by a hypothec. These future obligations are no longer confined to line of credit, but to any obligation whatsoever.[32]

To fully understand the intentions of the Québec legislator on the scope of the mortgage with regard to present and future obligations, we offer the following brief historical sketch of these transformations and how they have changed the relationship between mortgages and future obligations. We will then discuss the current legislative situation of the immovable hypothec regarding present and future obligations.

6.1 The immovable hypothec under the Civil Code of Lower Canada

In the *Civil Code of Lower Canada* (hereinafter *CCLC*) immovable hypothecs are governed by arts. 2016 and 2017.[33] They may be conventional, legal or judicial.[34] The hypothec is a

[30] In 1955, the Quebec government undertook the reform of the *Civil Code*. Over the years an administrative structure was set in place: l'Office de révision du Code civil. [..] During that time, specific legislation was adopted that significantly modified the *Civil Code* and demonstrated the importance of revising it to ensure that it reflects the values of contemporary Quebec society. [...] On 18 December 1990, the Minister of Justice introduced *Bill 125,* the draft *Civil Code of Québec*, which incorporated the earlier texts, revised and corrected in the light of all comments received in response to extensive consultation with various interested parties. [...] The *Civil Code of Quebec* was unanimously adopted on December 18, 1991. *Commentaires du ministre de la justice, Tome 1, Publications du Québec.*

[31] Arts. 2644-2802 CCQ

[32] Art. 2687 CCQ

A hypothec may be granted to secure any obligation whatever.

Art. 2697:

A hypothec is extinguished by the extinction of the obligation whose performance it secures. In the case of a line of credit or in any other case where the debtor obligates himself again under a provision of the deed of hypothec, the hypothec, unless cancelled, subsists notwithstanding the extinction of the obligation.

[33] Art. 2016 CCLC

real and accessory right. It gives its holder, usually the creditor, a right to the immoveable. The real right of the creditor consists in his ability to seize the immovable to ensure repayment of his debt.[35] According Mazeaud, an author specializing in civil law in the era when the *CCLC* was still in force, an immovable hypothec is:

> [TRANSLATION] a security which, while not authorizing divestiture, allows the creditor, if not paid by the end of the contractual term, to seize the property and follow it into the hands of whomsoever it may be.[36]

The hypothec confers a right of preference in the collocation of the debt and the right to follow. This means that the debitor retains full enjoyment of his property and retains full ownership. He can charge it (servitudes, right of use, a second mortgage) and can alienate it (sell, transfer, etc.).[37]

The accessory nature of the hypothec and specificity principle under the *CCLC*

A hypothec is a real and accessory right; it does not admit of any dismemberment of ownership.[38] In that era, the courts rigorously applied the accessory nature of the mortgage. Experts in civil law supported this line of thinking. The mortgage could not exist without the concurrence of a secured and determined obligation.[39] The accessory status of the hypothec is fundamental. Consequently, when the principal obligation is extinguished, the mortgage ceases to exist. On the other hand, the opposite does not automatically follow. A hypothec may cease to exist, but the claim (debt) may still remain.[40] It is important to distinguish between these two notions. The hypothec is a real, accessory right, and the claim is a principal, personal, moveable right.[41]

To be secured, the claim had to be certain and determined and the property offered as security had to be described. A general hypothec could not be created both against a building and against the *situs* of the building and be charged only against the debt to be

Hypothec is a real right upon immoveables made liable for the fulfilment of an obligation, in virtue of which the creditor may cause them to be sold in the hands of whomsoever they may be, and have a preference upon the proceeds of the sale in order of date as fixed by this code.

[34] Pierre Ciotola, *Les sûretés*, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 276

[35] Pierre-Claude Lafond, *Précis de droit des biens*, 2nd ed., Montreal, Les Éditions Thémis, 2007, p.167

[36] Pierre Ciotola., *Les sûretés,* 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 276

[37] Pierre Ciotola., *Les sûretés*, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 277

[38] Pothier defines it as follows: [TRANSLATION] "the mortgage cannot exist unless a principal obligation is secured. Accordingly, when the principal obligation is extinguished, as an accessory, so is the hypothec." See Louis Payette, "Des priorités et des hypothèques" in *La Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.91

[39] See Louis Payette, "Des priorités et des hypothèques" in *La Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.91

[40] Pierre Ciotola., Les sûretés, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 278

[41] Pierre Ciotola., Les sûretés, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 278

secured. This is the concept of the specificity of the mortgage.[42] The mortgage was valid only if it stated the certain and determinate sum for which it was constituted.[43] This specificity was in favour of the debtor so that he could pledge his credit to a single creditor. It favoured the collocation of the claim for the creditor. A person could still impose an obligation to do or not do. In this situation, the deed of hypothec had to stipulate a certain and determinate sum representing the value of this obligation.[44]

According to the principle of specificity, it was crucial that the amount of the security be specified in the deed to the extent of the sum for which the security was granted. Otherwise, the hypothec would be null and void.[45] The extent of the hypothec must in turn be specified in the deed together with all terms and conditions that could affect the security, for example, suspensive or resolutory conditions.[46] The only exception to this fundamental principle that exists in the *CCLC* is to be found in art. 2044.[47] In fact, it was possible for a hypothec to secure a future obligation, but only in the case of a line of credit. This took effect on the date of registration in the land register and not that of the advances made under this line of credit.[48]

The jurisprudence of the time seemed divided on this point. Some courts supported the rigid interpretation of Pothier, while others attempted to be more flexible by agreeing to hypothecate future obligations. Certain laws in the early 20th century, including the *Companies Act,*[49] were amended to allow the creation of hypothecs that could secure unissued obligations. These amendments were made to offset differing decisions about the accessory right of the hypothec.[50]

Despite the importance that *CCLC* appears to accord to the rule of specificity of the hypothec, it was not until 1984[51] that its scope with regard to the identification of the

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[42] Art. 2042 *CCLC*:
Conventional hypothecs are not valid unless the deed specially describes the immoveable hypothecated, with a designation of the coterminous lands, or of the number or name under which it is known, or of the lot or part of the lot and range, or of its number upon the plan and book of reference of the registry office, if such plan and book of reference exist.
[43] Pierre Ciotola., *Les sûretés*, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 285
[44] Pierre Ciotola., *Les sûretés*, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 295
[45] Pierre Ciotola., *Les sûretés*, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 294
[46] Pierre Ciotola., *Les sûretés*, 2nd ed., Montreal, Les Éditions Thémis, 1987, p. 294
[47] Art. 2044 *CCLC*:
Conventional hypothecs are likewise not valid unless the sum for which they are granted is certain and determined by the deed.
This provision does not extend to life-rents or other obligations appreciable in money, which are stipulated in gifts inter vivos.
[48] Louis Payette, *"*Des priorités et des hypothèques*"* in *La Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.91
[49] Louis Payette, *"*Des priorités et des hypothèques*"* in *La Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.91
[50] Louis Payette, *"*Des priorités et des hypothèques*"* in L*a Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.91
[51] Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) 97 *R. du. N. 450 (electronic document, no pagination)*

secured claim was first commented on by the courts, in *Banque Mercantile du Canada v. Yves Germain inc.*[52] In this case,[53] the Court acknowledged the validity of the hypothec with regard to the line of credit to which the hypothec referred. There is no indication in the clause that stipulates that the claim must be clear and precise. The hypothec is therefore valid inasmuch as the amounts were advanced under the line of credit. On the other hand, the Court declared the security on the hypothec to be invalid with regard to direct sums that were not advanced under the line of credit; since these do not correspond to the line of credit, their causes were not elaborated in the deed. In fact, the principle of the specificity of the hypothec makes the security invalid on any of the debtor's debts. Art. 2044. *CCLC* does not require the amount of the debt to be acknowledged in the constituting instrument, just the amount of the hypothec. The mere mention of the amount of the hypothec does not satisfy the principle of specificity.

This judgment and the confusion created by the courts over accessory rights and specificity probably influenced the legislature in the reform of the *Civil Code*. At that time, there was little information on the debt to be secured and it did not occur to the practitioners that the claim could not be determined within a deed of hypothec.[54] The question of determining the debt to be secured was raised when the financial institutions began making ever greater demands in mortgage applications.[55] Faced with an increasingly unstable real estate and financial market, the financial institutions decided to start providing mortgages covering present and future debts, both identified and unidentified.[56]

6.1.1 The hypothec under the *Civil Code of Québec*

The immovable hypothec remains a real accessory right (2660) to be granted by a notarial and consensual act(2693) and can secure any obligation whatsoever. (2687). It always confers a preferential right on the creditor as well as the right to follow.

6.1.2 A new exception is added to the principle of accessory right: Article 2797

Following the reform, the *Civil Code* created an exception to the general rule that the accessory follows the principal. This is article 2797.

> A hypothec is extinguished by the extinction of the obligation whose performance it secures.

[52] *Banque Mercantile du Canada v. Yves Germain inc*, [1984] C.S. 856

[53] In this case, the hypothec stipulated repayment of amounts paid or to be paid through a revolving line of credit. The creditor claimed the sum, part of which had been advanced through a line of credit, but of which the overdraft was not the result. The debtor invoked the principle of the specificity of the hypothec.

[54] Jacques Auger, "L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante," (1995) 97 *R. du. N. 450*

[55] Jacques Auger, "L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante," (1995) 97 *R. du. N. 450*

[56] Jacques Auger, "L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante," (1995) 97 *R. du. N. 450*

> In the case of a line of credit or in any other case where the debtor obligates himself again under a provision of the deed of hypothec, the hypothec, unless cancelled, subsists notwithstanding the extinction of the obligation.

In adopting this article, the legislator intended to fill a gap in the law, as can be seen in these comments by the Minister of Justice:

> [TRANSLATION] The first part of this article reflects point 5 of Art. 2081 *CCLC*: the hypothec is extinguished when the obligation that supports it is extinguished. The second part of the article is an exception to this general rule and thus fills a gap in the previous law. Indeed, it is possible that that the parties might want the amount of the obligation to be increased , and that its repayment be secured by the first security, as is the case with a line of credit. But beside this exception, it may be concluded that the hypothec is extinguished upon payment. [57]

Line of credit is no longer the only exception to the accessory rule. The legislator intended it to extend to all situations stipulated within the deed of hypothec that would permit the debtor to assume new obligations after repaying the principal on the loan.[58] Were it not for this exception, it might be concluded that the mortgage is extinguished when the principal obligation has been fully performed.[59]

The purpose of Article 2797 is to facilitate the borrowing of future sums. The debtor borrows a principal sum, for example the amount he needs to acquire his new property, pays it back, then borrows once again, still under the first hypothec.[60] Whether it takes the form of a line of credit, revolving credit, or any other provision that allows a debtor to contract a new debt with the same creditor, the latter remains assured of a continued hypothec on the property.[61]

The only condition made by the *Civil Code* is that the constituting act must stipulate that it is possible to borrow money in the future, with the hypothec as security. The value of the obligation to be secured may be indeterminate or indeterminable and may not even exist at the time the hypothec was constituted.[62] The debtor may request the cancellation of his hypothec if the creditor fails to perform his obligations as set forth in the act, that is to say, if he does not agree to lend the amounts requested by the debtor, despite the repayment of his original loan.[63]

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[57] *Commentaires du ministre de la justice, tome II*, Publications du Québec, Section 2797

[58] See Louis Payette, *"*Des priorités et des hypothèques*"* in *La Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.149

[59] *Commentaires du ministre de la justice, tome II,* Publications du Québec, article 2797, see Edith Lambert, *Les sûretés : extraits du Droit civil en ligne, Cowansville, Les Éditions Yvon*. Blais, 2009, analyse de l'article 2797, p.1023

[60] See Louis Payette, *"*Des priorités et des hypothèques*"* in L*a Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec*, Les Presses de l'Université Laval, 1993, p.150

[61] Louis Payette, *Les sûretés réelles dans le Code civil du Québec* 4th ed. Cowansville, Les Éditions Yvon Blais, 2010, p. 310

[62] Louis Payette, *"*Des priorités et des hypothèques*"* in La Réforme du Code civil, textes réunis par le Barreau du Québec et la Chambres des notaires du Québec, Les Presses de l'Université Laval, 1993, p.151

[63] Marc Boudreault, *Les Sûretés*, 3e éd., Montreal, Chambre des notaires du Québec, 2008 p.58

6.1.3 The specificity of the hypothec and unidentified future obligations

The adoption of the *CCQ* sparked a doctrinal controversy in Québec. There was general consensus regarding the ability of a debtor to hypothecate a property for present and future obligations. The controversy revolved mostly around the possibility of securing future obligations that were not identified at the time the hypothec was constituted. Based on the principle of the accessory, some authors thought it would be in fact impossible to take out a hypothec on future unidentified sums.[64] In fact, a hypothec assigned to unidentified future obligations would go against the principle of Art. 2661.[65]

Admittedly, as Louis Payette points out, a rigorous interpretation of the accessory nature of the hypothec does not permit it to secure future obligations, since the hypothec has no life without the concomitant existence of a principal obligation.[66] Thus, no hypothec can be created before the creation of the concomitant obligation. On the other hand, the *CCQ* does not require the hypothec and secured obligation to be created at the same moment.[67]

Some writers, including Jacques Auger,[68] claimed it was necessary to apply the strict rule of the specificity of the mortgage, namely, the specificity of the secured immoveable and that of the secured claim. The line of credit[69] referred to in Art. 2797 is certainly a potential future obligation, but is identifiable by its legal object. Accordingly, Auger stresses that for the obligation to be valid, it must satisfy the criteria of Art. 1373 para 2.

> **Art. 1373.** The object of an obligation is the prestation that the debtor is bound to render to the creditor and which consists in doing or not doing something. The debtor is bound to render **<u>a prestation that is possible and determinate or determinable</u>** and that is neither forbidden by law nor contrary to public order.

The specificity of the hypothec therefore requires that the obligation be identified. This prevents the debtor from irremediably compromising his credit standing, and allows third parties to the legal contract to know the debtor's situation with regard to the hypothec. If the future obligations to which the borrower consents are unidentified, the creditor will hold a permanent hypothec that secures the performance of all present and

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[64] Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) 97 *R. du. N.* 450

[65] Article 2661

A hypothec is merely an accessory right, and subsists only as long as the obligation whose performance it secures continues to exist.

[66] Louis Payette, *Les sûretés réelles dans le Code civil du Québec* 4th ed.157

[67] Art. 2797 *CCQ*

[68] Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) 97 *R. du. N. 450*

[69] [TRANSLATION] While not described within the *Civil Code*, a line of credit means any agreement whereby one party repeatedly has the power to engage the credit of the other or to incur debts against him. Must be interpreted broadly: line of credit, revolving credit, etc. In certain financial arrangements, the amount for which the second rank mortgage (umbrella, blanket or wrap-around mortgage) is granted includes the notional value of the balance of the first rank mortgage in addition to the capital amount of the loan granted by the second rank creditor. Louis Payette, *Les sûretés réelles dans le Code civil du Québec* 4th ed. Cowansville, Les Éditions Yvon Blais, 2010, , p. 310,

future debts, which is not in the debtor's interest.[70] This goes against the accessory principle, since the hypothec becomes a super security that is totally independent of the principal debt.[71]

Louis Payette[72] points out that a distinction needs to be made between two concepts: the principal obligation secured by the hypothec and the amount for which the constituting instrument states that the hypothec is consented.[73] It is not essential for the portion of the obligation to be determinate or even determinable[74] at the time the hypothec is constituted; it is sufficient that the debt has fallen due and is payable at the time the creditor intends to pursue his remedies.[75] The value of the obligation may be indeterminate or indeterminable, but it does not need to exist at the time the mortgage is created. Art. 2797 does not restrict the ability to create an immovable hypothec for unspecified future obligations to lines of credit and to deeds providing for the issue of obligations, as stipulated in the former law.[76]

St-Jacques v. Charbonneau[77] and *HSBC*[78] settled the issue of undetermined obligations. The rulings in these cases overturned the decision in *Mercantile Bank of Canada v. Yves Germain,*[79] which required, in order for the principle of specificity of the hypothec to be respected, that the hypothec include a reference to the secured obligation or the nature or cause thereof. In *St-Jacques v. Charbonneau*, the justices of the Québec Court of Appeal concurred with the opinion of Louis Payette quoted above. In fact, as stated in

[70] Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) 97 *R. du. N. 450,*

[71] Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) 97 *R. du. N. 450*,

[72] Louis Payette, *Les sûretés réelles dans le Code civil du Québec* 4th ed. Cowansville, Les Éditions Yvon Blais, 2010, p.309

[73] Louis Payette, L*es sûretés réelles dans le Code civil du Québec* 4th ed. Cowansville, Les Éditions Yvon Blais, 2010, p.303

[74] Vincent Karim. *Les obligations, vol 1*, 3rd ed. Montreal, Les Éditions Wilson & Lafleur, 2010
The legislator requires in the second paragraph of art. 1373 *CCQ,* that the prestation be possible, determinate or determinable, and that it continue to be so. In addition, ***in order for it to be determinable, the contract must stipulate the criteria for being so. Thus, it is not necessary that the price be fixed for an obligation to be valid. In fact, by using the words "determinate or determinable," the legislator suggests that a price that is not determined at the time of conclusion does not invalidate the obligation, provided that the price is determinable when the creditor demands its performance by the debto***r.

[75] Louis Payette, *Les sûretés réelles dans le Code civil du Québe*c 4th ed. Cowansville, Les Éditions Yvon Blais, 2010, p. 303

[76] Les sûretés réelles dans le Code civil du Québec 4th ed. Cowansville, Les Éditions Yvon Blais, 2010, p. 310

[77] *St-Jacques v. Charbonneau,*. C.A. Montreal, 500-09-001136-944, J.E., 99-944, (C.A.), analysis by Yvan Desjardins in Yvan Desjardins, *"*Le principe de la spécialité de l'hypothèque rejeté par la Cour d'appel *"* (2000), *R du N*. 102p. 441-445

[78] *Banque HSBC Canada v. 9082-3659 Québec inc*., [2005] *R.D.* I. 339 (C .S.)

[79] *Banque Mercantile du Canada v. Yves Germain inc*, [1984] C.S. 856, analysis in Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) *97 R. du. N. 450*

the decision,[80] art. 2797 does not require that the principal obligation be described in the act. It contains no specific requirement in this regard concerning present and future obligations.

In *St-Jacques* and *HSBC*,[81] the Court of Appeal and the Superior Court ruled that the specificity of the hypothec does not apply to the principal obligation. This does not harm any of the parties' future obligations, since the amount corresponding to the preference threshold is found in the documents filed in the appropriate register.[82] The deed of hypothec must contain the elements permitting the obligations to be identified: this follows from the very nature of a security. It is essential that the surety be attached to a secured obligation.[83] A clause that stipulates that the hypothec may secure not only the sums advanced by the creditor, but also any future sums that the debtor may subsequently contract with the same creditor, is perfectly valid.[84]

In short, the *CCQ* applies the rule of specificity to the limits of the right of preference and to the charged property. On the other hand, art. 2949[85] weakens this interpretation by permitting the hypothec to secure future real property in the constituting instrument without providing a description. Nor does the *Code* contain any rule regarding the specificity of the principal secured obligation.

Art. 2797 consecrates a practice that was current in the days of the *CCLC*, but was not framed by law: in the hypothecation of obligations or securities, it was not uncommon to create securities as collateral and continuous security against the borrower's present and future obligations.[86] It was stipulated that the hypothec constituted a continuous

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[80] *St-Jacques v. Charbonneau*, C.A. Montreal, 500-09-001136-944, J.E., 99-944, (C.A.), analysis by Yvan Desjardins, in Yvan Desjardins, *"*Le principe de la spécialité de l'hypothèque rejeté par la Cour d'appel *"* (2000), *R du N.* 102 pp. 441-445

[81] *St-Jacques v. Charbonneau,* C.A. Montreal, 500-09-001136-944, J.E., 99-944, (C.A.), and *Banque HSBC Canada v. 9082-3659 Québec inc*., [2005] R.D. I. 339 (C.S)

[82] Yvan Desjardins, in Yvan Desjardins, *"*Le principe de la spécialité de l'hypothèque rejeté par la Cour d'appel *"* (2000), R du N. 102 p. 443

[83] Yvan Desjardins, in Yvan Desjardins, *"*Le principe de la spécialité de l'hypothèque rejeté par la Cour d'appel*"* (2000), R du N. 102 p. 443

[84] A clause providing that the mortgage secures all *"*other liabilities, present or future, direct or indirect*"* was deemed good and sufficient for extending the mortgage to a deposit previously consented to as security against the debt of a third party toward the same creditor*. Banque HSBC Canada v. 9082-3659 Québec inc*., [2005] R.D. I. 339 (C.S.)

[85] Article 2949 *CCQ*

A hypothec affecting a universality of immovables ranks, in respect of each immovable, only from the time of registration of the hypothec against each.

Registration of a hypothec against immovables acquired subsequently is obtained by presenting a notice containing the description of the immovable acquired and a reference to the act creating the hypothec, and setting forth the specific amount for which the hypothec was granted.

However, if the hypothec was not published in the land book for the registration division in which the immovable acquired subsequently is located, its registration is obtained by means of a summary of the act creating the hypothec, containing a description of the acquired immovable.

[86] Yvan Desjardins, in Yvan Desjardins, *"*Le principe de la spécialité de l'hypothèque rejeté par la Cour d'appel *"* (2000), *R du N. 102* p. 443

security that would subsist even if at times there was no debt.[87] Third parties are not at all harmed by this procedure since they have access to the land register and can inform themselves of the debtor's hypothecary debts.[88]

The constitutive instrument must specify the maximum amount to which the creditor would be entitled if he were to pursue his hypothecary remedies. Future amounts may be smaller or greater than this amount. The hypothec must specify the sum for which it is granted under pain of nullity. However, it does not have to specify the amount of the secured obligation; it only needs to specify the maximum amount of preferential rights attached to the hypothec.[89]

6.1.4 The extinction of the hypothec on future obligations

In principle, owing to its accessory nature, the hypothec is extinguished when the principal claim no longer exists. But what about hypothecs that secure present and future obligations? Under Art. 2797, the creditor is entitled to refuse an application to discharge the debtor through cancellation of the hypothec, even if the latter has completely repaid the principal loan.[90] In fact, his future obligations are still subject to the hypothec. Based on section 2797, the creditor may refuse to grant cancellation of the hypothec as long as all the debtor's other obligations toward the creditor or any third party assimilated to the creditor have not been fully paid.[91] The legislator permitted hypothecs to be continuous in nature.[92] It may be that at certain moments, the debtor owes the creditor nothing, yet the hypothec is not automatically extinguished. On the other hand, if the creditor decides to seize the property in payment, all the debtor's future obligations toward the creditor are erased.[93]

Prospective buyers need to pay particular attention to the hypothec on the property they wish to acquire, particularly its scope. The buyer of a building with a hypothec that secures a line of credit does not have the right to obtain cancellation upon payment of the balance due on the credit computed as of the date of acquisition: he must pay the maximum amount secured by the hypothec.[94] Financial institutions are generally agreed to grant a release from (or partial acquittance of) a hypothec. They will in fact be

[87] Louis Payette, *Les sûretés réelles dans le Code civil du Québec*, 4th ed. éd. Cowansville, Les Éditions Yvon Blais, 2010, p. 305

[88] *Banque Mercantile du Canada v. Yves Germain inc.*, [1984] C.S. 856 *St-Jacques v. Charbonneau*,. C.A. Montreal, 500-09-001136-944, J.E., 99-944, (C.A.), *Banque HSBC Canada v. 9082-3659 Québec inc*., [2005] *R.D.* I. 339 (C.S

[89] Louis Payette, *Les sûretés réelles dans le Code civil du Québec*, 4th ed. Cowansville, Les Éditions Yvon Blais, 2010; Jacques Auger, *"*L'hypothèque garantissant des obligations futures non identifiées : l'hypothèque volante,*"* (1995) 97 *R. du. N. 450*

[90] Marc Boudreault, « Sûretés » (2009) *R.du.N*. 11, p. 155 et seq.

[91] Marc Boudreault, « Sûretés » (2009) R.du.N. 11, p. 155 et seq.

[92] Louis Payette, *Les sûretés réelles dans le Code civil du Québec*, 4th ed. Cowansville, Les Éditions Yvon Blais, 2010 p.302

[93] Marc Boudreault, « Sûretés » (2009) R.du.N. 11, p. 155 et seq.

[94] Louis Payette, Les sûretés réelles dans le Code civil du Québec, 4th ed. Cowansville, Les Éditions Yvon Blais, 2010 p.405

reluctant to grant an acquittance,[95] since this would entail the complete erasure of the hypothec from the land register, and therefore the loss of the security on the property for the creditor.

6.1.5 Legal problems raised by art. 2797*CCQ*

Article 2797 appears to raise some legal problems. The debtor must remain vigilant and make sure that he is well informed by his bank. As Marc Boudreault points out, debtors are often poorly informed about the true extent of their mortgage,[96] which is not necessarily due to bad faith on the part of the mortgage grantor. The federal legislation governing banking institutions[97] requires disclosure of the cost of borrowing and interest rates, but does not require disclosure of the remaining clauses. The *Consumer Protection Act*[98] applies to a credit agreement attached to a mortgage, but its regulations exclude various sections of the *Act*. The only statutory requirement concerns the notary, who has the responsibility of advising consumers[99] and reading the documents[100] and ensuring that they have understood the extent of the contract and its consequences.

The deed of hypothec is an imperfect synallagmatic contract, by which the creditor has fewer obligations than the debtor. It is also, according to the criteria stated in art. 1379 *CCQ,* a contract of adhesion.[101]

The conventional hypothecary loan contract is usually a standardized pre-printed contract. The drafting of the main provisions of the contract is unilateral and imposed on the debtor, who usually has no choice but to accept them.[102] The mortgage lender is in a strong position to impose non-negotiable, abusive or unacceptable conditions.[103] This constitutes an imbalance of power, in both technical and economic terms. On the other hand, the fact that the hypothecary loan contract is a contract of adhesion does not necessarily make it illegal and abusive. To be legally valid, it is sufficient for the signing party to be aware of the clauses of the contract, including those strictly stipulated in favour of the creditor. Indeed, if the lender properly explains the content of the mortgage agreement to the borrower, the contract will not generally be vitiated by a lack of consent. For the mortgage lender, it is important to ensure that the borrower is made aware of the terms of the extent of his mortgage and understands the various definitions that apply. He must also explain the ins and outs of the constituents' commitments and those of third parties who are related to the creditors but are not specified in the contract.

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[95] Marc Boudreault, « Sûretés » (2009) R.du.N. 11, p. 155 et seq.
[96] Marc Boudreault, *Les Sûretés*, (2009) R.du.N. 11, p. 155 et seq.
[97] *Bank Act*, *Interest Act*, *Cost of Borrowing Regulations*
[98] *Consumer Protection Act,* RSQ, c P-40.1
[99] *Notarial Act*, RSQ, c. N-3, s. 11,
[100] *Notarial Act*, RSQ, c N-3, s. 51
[101] Article 1379 : A contract of adhesion is a contract in which the essential stipulations were imposed or drawn up by one of the parties, on his behalf or upon his instructions, and were not negotiable. Any contract that is not a contract of adhesion is a contract by mutual agreement.
[102] François Lebreux, *"*L' étendue de l'hypothèque et ses conséquences*"* (2008) *C.P.* p.67
[103] François Lebreux, *"*L' étendue de l'hypothèque et ses conséquences*"* (2008) *C.P.* p.68

If the creditor decides to draw up a contract or clause that is external to the mortgage contract for future obligations, he must expressly inform the debtor of the existence of such an external clause or agreement, lest it be annulled by the court.[104] Moreover, the rate of interest applicable on future obligations is generally different from that applied to the hypothec on the building, which nonetheless secures such obligations. In fact, the interest rate will be different for each obligation. This rate is generally higher than that agreed to for the principal loan secured by the hypothec. These various requirements make it difficult to apply sections 6, 8 and 10 of the *Interest Act*. Should they be applied to each of the obligations, only to the principal loan or to the whole?

There is also the problem raised in the previous section, that of cancelling the hypothec on future obligations. For the debtor, it may be difficult, if not impossible, to obtain discharge.[105]

Finally, our analysis of the legislation research has led us to observe that the mortgage contract, which is a contract of adhesion, will be valid as long as the debtor has consented to, and has understood, its essential terms and conditions. The creditor must be careful when drafting the terms of the contract since they may be invalid if they are illegible and incomprehensible to a reasonable person, and are detrimental to the debtor.[106]

[104] François Lebreux, *"*L' étendue de l'hypothèque et ses conséquences*"* (2008) *C. P.* p.70
Article 1435 *CCQ*
An external clause referred to in a contract is binding on the parties.
In a consumer contract or a contract of adhesion, however, an external clause is null if, at the time of formation of the contract, it was not expressly brought to the attention of the consumer or adhering party, unless the other party proves that the consumer or adhering party otherwise knew of it.

[105] Marc BOUDREAULT, *"*Sûretés,*"* (2009) *R.du.N.,* 11, p.155 et seq.

[106] Article 1437 CCQ
An abusive clause in a consumer contract or contract of adhesion is null, or the obligation arising from it may be reduced.
An abusive clause is a clause which is excessively and unreasonably detrimental to the consumer or the adhering party and is therefore not in good faith; in particular, a clause which so departs from the fundamental obligations arising from the rules normally governing the contract that it changes the nature of the contract is an abusive clause.

7. Real rights and property rights in common law and the notion of right of ownership

Before beginning our study of the mortgage in the other provinces of Canada and mortgages that secure future obligations, we want to give a brief summary of the theory of real property in common law as well as the notion of ownership. In fact, there are notable differences between the civil law regime of real rights and the common law regime of real rights. This short presentation will be useful in the analysis of the traditional mortgage and the hypothec and will provide a fuller understanding of what is covered by the mortgage security.

7.1 The doctrine of estates

Under common law, the right of absolute ownership of a thing does not exist. There is only a right over the estate of the land. The land belongs to the Crown (the State) and the estate to individuals.[107] Several people, called tenants, may own the same estate. This division of territory is a legacy from the feudal[108] era. While civil law is based largely on Roman law, common law has developed a separate system of property law based on the doctrine of estates.[109]

The doctrine permits the exercise of a plurality of real rights or real interests over a single property.[110] In fact, it is the concept of the estate that most closely resembles that of real right of ownership in the civil law regime. It is the right that the person holds in the land and can use as security against the sum lent by the mortgagee. Estates are grouped into different categories and owners' rights vary depending on the category to which the estate belongs.[111]

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[107] Barbara Pierre, *"*Classification of Property and Conceptions of Ownership in Civil and Common Law. *"* (1997) 28 *R.G.D.* p.242

[108] Louise Bélanger-Hardy, Aline Grenon, *"*Éléments de common law canadienne : comparaison avec le droit civil québécois,*"* Toronto, Thomson/Carswell, 2008, p.106, Barbara Pierre, *"*Classification of Property and Conceptions of Ownership in Civil and common law. *"* (1997) 28 *R.G.D.* pp. 242-243

[109] Louise Bélanger-Hardy, Aline Grenon, *"*Éléments de common law canadienne : comparaison avec le droit civil québécois,*"* Toronto, Thomson/Carswell, 2008, p.106, Barbara Pierre, *"*Classification of Property and Conceptions of Ownership in Civil and common law. *"* (1997) 28 *R.G.D* p. 114

[110] Louise Bélanger-Hardy, Aline Grenon, Éléments de common law canadienne : comparaison avec le droit civil québécois, Toronto, Thomson/Carswell, 2008, p.114

[111] Estates and fees:

- Freehold: any interest in real property which is a life estate or of uncertain or undetermined duration (having no stated end). Divided into fee simple and fee tail.
- Fee simple: absolute title to land, free of any other claims against the title, which one can sell or pass to another by will or inheritance. Also called *"*ownership.*"*
- Fee tail: can endure until the holder dies without surviving issue, but it cannot be passed on to collateral heirs. Cannot be hypothecated. Canada has abolished the fee tail estate since it restricts the ready alienation, or transfer, of property, and has transformed it into a fee simple through statute.

A future (or estate) interest is an interest in the property that comes into being when there is incomplete transfer of the estate.[112] The best example to describe future interest is the mortgagor's right to an equity of redemption[113] of his estate. In fact, during the mortgage transaction, the creditor holds legal title to the estate, but the debtor retains equitable title. This title may be further alienated or encumbered by the debtor. The creditor and the debtor both find themselves with a part of the estate. We may thus see a string of future interests in the same estate. In common law, there is relativity of real rights. This concept allows for the creation of chains of successive domains that increase the real rights on the same property. Relativity is threefold in that it comprises: the feudal structure (estates and fiefs), future interests (legal title and equitable title) and the relativity of title.[114]

7.1.1 The concept of property in common law

The right of property in common law includes the estate and the obligations attached to it.[115] These obligations have been modified over time and have been restricted by legislation.[116] The major reform of ownership of 1925 introduced a new definition of property rights.

> […]the fundamental principles of the law of ownership of land remain the same as before the legislation of 1925. Land is still the object of feudal tenure; the Sovereign remains the lord paramount of all the land within the realm; every parcel of land is still held of some lord [...I and the greatest interest which any subject can have in land is still an estate in fee simple and no more [117]

As we can see, the concept of ownership in common law does not depend on a direct interest in the property, unlike in civil law.[118] The estate does not confer the right of preference or the right to follow.[119] These interests in the land are binding on the parties having contracted a hypothec, a charge, a lien or a pledge. These interests do not follow

[112] Louise Bélanger-Hardy, Aline Grenon, "Éléments de common law canadienne : comparaison avec le droit civil québécois," Toronto, Thomson/Carswell, 2008, p.119

[113] Louise Bélanger-Hardy, Aline Grenon, "Éléments de common law canadienne : comparaison avec le droit civil québécois," Toronto, Thomson/Carswell, 2008, p.121

[114] Louise Bélanger-Hardy, Aline Grenon, "Éléments de common law canadienne : comparaison avec le droit civil québécois," Toronto, Thomson/Carswell, 2008, p.131

[115] Barbara Pierre, "Classification of Property and Conceptions of Ownership in Civil and Common Law. " (1997) 28 *R.G.D.* p.250

[116] Barbara Pierre, "Classification of Property and Conceptions of Ownership in Civil and Common Law. " (1997) 28 *R.G.D.* p.250

[117] C. Williams, "The fundamental principles of the present law of ownership of land" (1931) 75 S.J. 848 in Barbara Pierre, "Classification of Property and Conceptions of Ownership in Civil and Common Law." (1997) 28 *R.G.D.* p.250

[118] Barbara Pierre, "Classification of Property and Conceptions of Ownership in Civil and Common Law. " (1997) 28 *R.G.D.* p.251

[119] Barbara Pierre, "Classification of Property and Conceptions of Ownership in Civil and Common Law. " (1997) 28 *R.G.D.* p.251

the property, they follow persons.[120] Since 1926, there has been only one estate that could give rise to legal title: the fee simple, which gives absolute title to the estate.[121]

7.2 The common law mortgage: the Littleton's classic mortgage

The classic common law mortgage[122] dates from the fifteenth century, at which time the immovable security became a fixed operation.[123] The original mortgage transaction involved a debtor (borrower) and a creditor (lender). The mortgagor transferred his interest in the land to his creditor on the express condition that total payment would cancel this transfer.[124] The debtor physically transferred the property, which included not just the title, but also the estate that was the subject of the transfer.[125]

The creditor held the property for as long as it was not repaid under the terms of the deed. After performing his obligations, the debtor could take possession of his land. On the other hand, if he failed to pay his obligations in due course, the land was forever removed from his estate and became the absolute property of the creditor. The debtor's property was used as collateral to secure his loan or obligation to the creditor. The debtor's only property rights were to redeem the land and take possession of it upon termination of the mortgage. If, due to some misfortune, the debtor failed to pay his debt by the time specified in the mortgage agreement, he lost his land forever.[126]

Since the 18th century, the debtor has been able to retain possession of the mortgaged premises. It was then that the clause of right of peaceful possession of property was introduced. This clause is still included in mortgage contracts today. The debtor has the right to peaceful possession of the property for as long as he satisfies the terms of the

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[120] Barbara Pierre, *"Classification of Property and Conceptions of Ownership in Civil and Common Law,"* (1997) 28 *R.G.D.* p.251

[121] Barbara Pierre, *"Classification of Property and Conceptions of Ownership in Civil and Common Law,"* (1997) 28 *R.G.D.* p.256
The owner of the fee simple estate may alienate, encumber, assign, it etc. These alienations will result in rights to the equitable title. Thus, one estate may have several owners: the holder of the legal title and those of the equitable title[121]

[122] There are three essential elements of the classic common law mortgage, which were determined in *Santley v. Wilde* ([1899] 68 L.J, ch. 2): it must first of all contain a contract for the transfer of property,. Second, this transfer must secure payment of a debt or the performance of an obligation. Third, the mortgage must contain a clause that reconveys the land to the debtor's estate when the latter has discharged all his obligations.

[123] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991, p. 21 and John Delatre Falconbridge, W.B. Rayner, Richard H, McLaren, Falconbridge on Mortgages, 4th ed., Agincourt, Canada Law Book, 1977, p.7

[124] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991

[125] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991, p. 22,
The properties that can be mortgaged are fee simple estates, fee tail estates life estates and leasehold estates.

[126] Bruce H. Ziff, *Principles of Property Law*, 5th ed., Toronto, Carswell, 2010, p.433 and Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991, p. 22,

mortgage agreement.[127] The classic common law mortgage process, therefore, was similar to pawning a property, since the debtor pledged his land against a sum of money and could only get it back by repaying the entire debt.[128] To this pledge of property was added the pledge of peaceful possession, since the mortgagee retained, despite having transferred ownership,[129] the right of peaceful use of his land and the enjoyment of its fruits and revenues. In addition, any profits realized could not be applied to reducing the debt.[130]

After repaying the entire debt, the land was not automatically reassigned to the debtor; he has to obtain what is known as a certificate of discharge. The creditor was obliged to grant the certificate if the debtor had in fact fulfilled his commitments. If he refused to comply with this request, then the debtor could file a suit in accordance with his right of redemption .[131]

7.3 Introduction of the charge: the contribution of equity

The classic Littleton mortgage was substantially transformed by the inclusion of equity, namely, the debtor's right of redemption. The definition given in Littleton gave creditors ample opportunity for abuse.[132] In fact, in the sixteenth and seventeenth centuries, mortgages were usually consented to by debtors who found themselves in a very precarious financial situation. Creditors enjoyed far greater economic power than debtors.[133] The Court of Chancery and other courts of equity had jurisdiction to protect debtors from usurious creditors and afforded legal recourse to debtors who not could meet their obligations in time and place.[134]

As of the 17th century, the Court extended its jurisdiction in equity to protecting any debtors who found themselves in a situation in which the mortgage agreement included a penal clause, even if no particular motive could be invoked to justify its intervention.[135] Previously only customary, the right of redemption now became an established concept: the doctrine of equity was born.[136] This right was then imposed as a fundamental principle of the mortgage. The creditor became the owner of the estate upon the constitution of the mortgage, but the debtor had the right of redemption once he had

[127] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p.37
[128] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 22
[129] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p.22
[130] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p.22
[131] Joseph E. Roach, L*es hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 8
[132] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 99
[133] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 99
[134] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 100
[135] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 100
[136] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 100

repaid his debt, even if he did not meet the deadline stipulated by the mortgage. As long as the creditor remained inactive, i.e. he did not pursue any of his remedies, the right of redemption remained valid.[137] The lawsuit filed by the creditor[138] automatically activated the debtor's right of redemption.

7.4 Equity and the right of redemption

The right of redemption is a real property right since the debtor becomes the holder of equitable title, subject to the rights conferred on the creditor under common law.[139] The debtor had the right to reconveyance legal title, in the case of a first mortgages, and to the equitable title in the case of second mortgages.[140] He could assign, alienate or mortgage it. Courts of equity developed a set of rules to protect debtors against the abuses of creditors. The debtor now had an absolute right of redemption: it could not be lost or waived by an agreement. It was a fundamental right.

On the other hand, the right of redemption created a certain inequality for the creditor, who found himself faced with a debtor who could recover the security regardless of whether he was in default or if the term had expired. It was then concluded that the creditor could terminate the debtor's right of redemption by default by filing a petition for foreclosure with the court[141].

7.4.1 The anti-clogging doctrine

Despite this new protection, the Court held that the equitable right of redemption was not sufficiently robust to protect the debtor. In fact, some creditors tried to impede this fundamental right by subverting the rules of right of redemption by means of an agreement terminating the right of redemption or by a disguised mortgage.[142] The Court then decided to create a set of rules that allowed a debtor to exercise his right to redeem freely and fully. This is the anti-clogging doctrine.[143] Divided into three broad principles, these rules were adopted to afford extended protection to the debtor. Although these rules have been relaxed in the case of commercial mortgage agreements, they should

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[137] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 100
[138] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 100
[139] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 23
Remedies available to the hypothecary creditor:
Foreclosure
Judicial sale
Extrajudicial sale
Possession
Stay of proceedings
[140] Joseph E. Roach, Les hypothèques immobilières en Common Law, Cowansville, Les Éditions Yvon Blais, 1991 p. 35
[141] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 101
[142] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 101. Disguised hypothecs make take the form of a sale with right of redemption or a sale with resolutory condition
[143] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 102.

always be followed by the mortgagee who lends a sum of money to an individual debtor, also known as a "protected person."[144]

A) "Once a mortgage, always a mortgage"

This maxim expresses at the very essence of the notion of equity. When the contract between the parties is deemed to be a mortgage, any clause aimed at overriding the debtor's right of redemption will be considered null and void.[145] This principle was enunciated very early in the 20th century in *Samuel v. Jarrah Timber and Wood Paving Corp Ltd*.[146]

> The doctrine "once a mortgage, always a mortgage" means that no contract between a mortgagor and a mortgagee made at the time of the mortgage and as part of a mortgage transaction, or, in other words, as one of the terms of the loan, can be valid if it prevents the mortgagor from getting back his property on paying off what is due on his security. Any bargain which has that effect is invalid, and is inconsistent with the transaction being a mortgage**.**[147]

As can be seen, this maxim has two components , namely, the existence of a mortgage – the mortgage must be established – and the debtor's inherent right to buy back the land.[148] The Court examines the essence of the contract, not its form. The mortgage must always remain consistent with its true nature, which is that of a security on a land.[149]

B) "The lender should have no collateral advantages"

This maxim corresponds to the traditional position of equity: the creditor may not enjoy a collateral benefit in the mortgage.[150] The creditor is usually not entitled to receive the benefits deriving from the security (rents, for example). All he is entitled to is the value of his security on the land. This interdiction was created a time when usurious lenders contrived to circumvent the rules by imposing interest on the debtor in order to obtain a

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[144] *"*The doctrine of clogs on the equity of redemption should be abolished generally. It should, however, be retained in part in respect of consumer transactions insofar as it would prevent options to purchase from being effective in respect of such mortgages.*"* Ontario Law Reform Commission, *The Law of Mortgages*, Toronto, Ministry of the Attorney General, 1987, p.29. Quoted in Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 102 p.114

[145]Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 103

[146] *Samuel v. Jarrah Timber and Wood Paving Corp. Ltd* [1904] A.C. 323, [1904] A.C. 329, [1903] 2 c. 1

[147] *Samuel v. Jarrah Timber and Wood Paving Corp. Ltd* [1904] A.C. 323, [1904] A.C. 329, [1903] 2 c.1 principle reaffirmed in *Dical Investments Ltd. C. Morrison* [1990] 75 O.R. (2d) 417, [1989] 68 O.R. (2E) 549 (Ont. H.C.J.). Quoted in Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 103

[148] *Wilson v. Ward*, [1930] S.C.R. 212, 24 Alta L.R. 48 [with references to S.C.R.]. Quoted in Joël Ménard-Cabelli., *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 104

[149]Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 103 p.104 principe affirmé dans *Cambell c. Holyland,* (1876) 7 Ch. D. 166, 47 L.J. Ch. 145.

[150] Joël Ménard-Cabelli, *"*La doctrine des entraves au droit de rachat*"* (1998-1999) 30 *R.D. Ottawa*, p. 106

portion of the revenues from his land in addition to the debt owed.[151] Over time, the courts have relaxed this rule, as this excerpt from *Krelinge* indicates.[152]

> In every case in which a stipulation by a mortgagee for a collateral advantage has, since the repeal of the usury laws, been held invalid, the stipulation has been opened to objection, either 1) because it was unconscionable, or 2) because it was in the nature of a penal clause clogging the equity arising on failure to exercise a contractual right to redeem, or 3) because it was in the nature of a condition repugnant as well to the contractual as to the equitable right.

Nowadays, certain additional clauses concerning collateral benefits may be added and accepted by the courts. These clauses must not impose excessive and exorbitant obligations on the debtor and may not impede the right of redemption.[153]

C) "There must be no stipulation in the mortgage that will fetter the property on redemption"

The last maxim refers to a collateral benefit that would extend beyond the term of the mortgage. Ever since *Kreglinger*,[154] it has been possible to extend a collateral benefit of the creditor beyond the term of the mortgage contract if this advantage does not impede the debtor's right of redemption. Moreover, if the parties wished by this collateral benefit to create an agreement exterior to the mortgage that would remain associated with the contract, such an independent agreement would be valid.[155]

Despite the laudable goals behind its inception, certain judges criticized the doctrine prohibiting clogs to the right of redemption. The rules were relaxed after judges found that it went well beyond the initial objective of protecting the debtor against a creditor taking over ownership of land in an absolute manner when the value of the latter was far higher than the value of the remaining debt.[156]

Ontario, incidentally, introduced reforms[157] aimed at eliminating any anomalies and anachronisms that the doctrine might occasion. The doctrine of impediments was gradually eliminated for commercial transactions. However, it was retained for ordinary debtors in order to prevent creditors from exploiting the imbalance of power by

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[151] Joël Ménard-Cabelli, "La doctrine des entraves au droit de rachat" (1998-1999) 30 *R.D. Ottawa*, p. 106

[152] *Kreglinger v. New Patagonia Meat and Storage Co. Ltd.,* [1914] A.C. 25, [1911-1913] All E. R. 970 (H. L.) [with references to aux A.C.]. Quoted in Joël Ménard-Cabelli, "La doctrine des entraves au droit de rachat" (1998-1999) 30 *R.D. Ottawa*, p. 103

[153] Joël Ménard-Cabelli, "La doctrine des entraves au droit de rachat" (1998-1999) 30 *R.D. Ottawa*, p. 106 inspired by *Biggs c. Hoddinott,* [1898] 2 ch. 307; [1895-9] All E.R. Rep.625.

[154] *Kreglinger v. New Patagonia Meat and Storage Co. Ltd*., [1914] A.C. 25, [1911-1913] All E. R. 970 (H. L.) [with references to A.C.]

[155] Joël Ménard-Cabelli, "La doctrine des entraves au droit de rachat" (1998-1999) 30 *R.D. Ottawa*, p. 109 It could therefore be concluded that it was *Kreglinger* that opened the way for mortgages securing futures obligations.

[156] Joël Ménard-Cabelli, "La doctrine des entraves au droit de rachat" (1998-1999) 30 *R.D. Ottawa*, p. 111

[157] Ontario Law Reform Commission, *The Law of Mortgages*, Toronto, Ministry of the Attorney General, 1987

converting the original mortgage into another transaction that was more advantageous to them.[158]

7.5 The mortgage since legislative reforms of provincial mortgage laws: the Torrens Lands Title System

In the 1980s, the common law provinces set about reforming mortgage rights.[159] In order to standardize the system of registration of real estate contracts and securities, the provinces gradually dropped their traditional system of land titles. They abandoned the former definition of the mortgage in favour of that of the "charge." Thecharge, unlike a mortgage, does not concede transfer of ownership of the land to the holder of the mortgage,[160] but rather transfers the legal title, which is subject to the debtor's right of redemption once the debt is fully repaid. Ontario and British Columbia still use the term mortgage, although the correct term is charge.[161]

The charge is a security interest that proceeds from the law. A charge is a statutory creation, which is to say that its essence is to be found in the particular laws of each province, each of which gives its own interpretation. The means by which is exercised and extinguished and the possible remedies are stipulated within each particular legislation.[162] It is therefore not governed by common law, but by the legislation that created it. A legal charge is a security on real property that is binding on the land but does not prevent transfer of title.[163] Rather, it gives the creditor legal title to the land. The charge has much in common with the civil law hypothec found in Québec.[164] The charge must never be confused with the common law mortgage.[165] The charge was established as a legal instrument by the Torrens Lands Title System. This system of title registration is in force in all the Canadian common law provinces, with the exception of Newfoundland-Labrador and Prince Edward Island.[166] Prince Edward Island, which kept the old system of registering deeds, Ontario, Manitoba and New Brunswick have a mixed

[158] Joël Ménard-Cabelli, "La doctrine des entraves au droit de rachat" (1998-1999) 30 *R.D. Ottawa*, p. 114
[159] Joseph E. Roach, *Les hypothèques immobilières en Common Law,* Cowansville, Les Éditions Yvon Blais, 1991 pp. 8-9
[160] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 pp. 9,11, The distinction was established in the Supreme Court decision *Smith v. National Trust*, (1912) S.C.R. 618
[161] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 pp. 8-9
[162] *Land Titles Act* CHAPTER L-1.1
25(2)The owner of a registered mortgage may enforce all rights and remedies permitted by law as if the lands had been conveyed to him by mortgage subject to a proviso for redemption.
[163] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 357
[164] Yaëll Emeraich, "Regard civiliste sur le droit des biens de la Common Law : pour une conception transsystémique de la propriété" (2008) 38 R.G.D., p.357
[165] *Smith v. National Trust*, (1912) 45 R.C.S. 618
[166] Joseph E. Roach, *The Canadian Law of Mortgages*, 2nd ed., Toronto, Butterworths, 2010, p.9

regime that involves registering both deeds and titles (Torrens). The western provinces are subject only to the Torrens system.

Henceforth, in all provinces using the Torrens system,[167] the charge or mortgage is extinguished the moment that the principal and interest are paid or when the obligation is discharged. The purpose of the certificate of discharge from the charge is simply to demonstrate to others that the mortgage debt has been paid.[168] The charge does not transfer the land to the creditor, but confers upon him the same remedies as the common law mortgage.[169] On the other hand, in order for the creditor to pursue the same remedies as those available under the common law mortgage, an express statutory provision must exist to this effect.[170]

The reform of land title registration and property rights legislation focused on standardizing the form of real estate sureties since the remedies available to both the creditor and the debtor remain the same as those allowed by the common law mortgage. Following the reform of the various land title systems, the charge becomes the most common form of real estate surety in Canada.[171]

Unlike the traditional system of registering deeds, the Torrens system is a system of registering titles. It is an adaptation of the Australian Torrens system.[172] The provinces that have adopted this system have created different variants based on their own needs.[173] The Torrens system offers more security than the traditional contract registration system. It secures the title, which becomes almost unshakable.[174]

Despite the advantages of the Torrens system, some provinces have decided to keep the system of registration of deeds or simply adopt a mix of the Torrens System and the traditional system. Since setting the Torrens System in motion involves such a long and expensive process, some provinces have opted to keep their old system rather than

[167] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 75

[168] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 76

[169] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 9,10, principle drawn from Kennedy c. Agricultural Dev. Bd. [1926] 59 O.L.R. 374, 4 D.L.R. 717

[170] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 426

[171] Joseph E. Roach, *The Canadian Law of Mortgages*, 2nd ed., Toronto, Butterworths, 2010, p.9

[172] Joseph E. Roach, *The Canadian Law of Mortgages, 2nd ed.,* Toronto, Butterworths, 2010, p.10

[173] Michel Bastarache, Andéa Boudreau-Ouellet, *Précis du droit des biens réels*, Cowansville, Les Éditions Yvon Blais, 1993, p.246: However, three main principles remain: accuracy, exclusivity and assurance. Accuracy requires that the certificate obtained faithfully reflect its contents and remains the true title of the owner. It is binding on all and confers absolute title. Exclusivity ensures that those inspecting the register do not have to take into account what does not appear in the certificate. These charges and other encumbrances are no longer relevant. The chain of title no longer need to be traced back. The Torrens system secures the title and gives the injured party the possibility of seeking redress.

[174] Michel Bastarache, Andéa Boudreau-Ouellet, Précis du droit des biens réels, Cowansville, Les Éditions Yvon Blais, 1993, p.246:

replace it with Torrens.[175] In this way, they permit registration to be carried out in both ways, but apply the definition of charge as adopted by the Torrens system.[176]

7.6 A mortgage that secures future obligations

A mortgage may be constituted on a freehold estate (fee simple or fee tail), on a life estate or on a leasehold estate. It secures all obligations and must respect the right of redemption. Our research has identified only one law that states explicitly that a mortgage can be used to secure present and future obligations. This is the *Real property Act,*[177]*,* in force in Manitoba. Does this mean that a debtor can never consent to mortgaging his land to secure future obligations? It would appear not. In fact, some provincial laws respecting property rights include a series of implied covenants[178] within

[175] Louise Bélanger-Hardy, Aline Grenon, *"*Éléments de common law canadienne : comparaison avec le droit civil québécois,*"* Toronto, Thomson/Carswell, 2008, p.165

[176] Louise Bélanger-Hardy, Aline Grenon, *"*Éléments de common law canadienne : comparaison avec le droit civil québécois,*"* Toronto, Thomson/Carswell, 2008, p.165

[177] The *Real Property Act,* CCSM c R30

[...]

In this Act, and in instruments purporting to be made or registered under this Act, unless the context otherwise requires

[...]

*"*mortgage*"* a charge on land created for securing a debt existing, future or contingent, or a loan, and includes an hypothecation of the charge; (« hypothèque »)

Interesting point to observe:

Meaning of *"*residential mortgage*"*

77.1(1) In this section and sections 77.2 and 77.3, *"*residential mortgage*"* means a mortgage that is registered against the residence where the borrower resides and is granted, entered into or assumed for the purpose of permitting the borrower

(a) to acquire the residence;

(b) to make improvements to the residence;

(c) to make expenditures for family or household purposes; or

(d) to re-finance for a purpose referred to in clauses (a) to (c).

[178] *Land Registration Reform Ac*t R.S.O. 1990, CHAPTER L.4 (Ontario)

Charge: implied covenants

7. (1) A charge in the prescribed form shall be deemed to include the following covenants by the chargor, for the chargor and the chargor's successors, with the chargee and the chargee's successors and assigns:

Usual covenants

1. In a charge of freehold or leasehold land by the beneficial owner:

i. That the chargor or the chargor's successors will pay, in the manner provided by the charge, the money and interest it secures, and will pay the taxes assessed against the land.

ii. That the chargor has the right to give the charge.

iii. That the chargor has not done, omitted or permitted anything whereby the land is or may be encumbered, except as the records of the land registry office disclose.

iv. That the chargor or the chargor's successors will insure the buildings on the land as specified in the charge.

v. That the chargee on default of payment for the number of days specified in the charge or in the Mortgages Act, whichever is longer, may on giving the notice specified in the charge or required by that Act, whichever is longer, enter on and take possession of, receive the rents and profits of, lease or sell the land.

the mortgage. Under the reform, the parties can change, negotiate or exclude these covenants. The parties must then submit a list of model clauses to the registrar or simply attach it to the mortgage document in compliance with their respective legislation.[179] These implied covenants relate to the rights and obligations of both parties to the contract.[180]

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vi. That where the chargee enters on and takes possession of the land on default as described in subparagraph v, the chargee shall have quiet enjoyment of the land.
vii. That the chargor or the chargor's successors will, on default, execute such assurances of the land and do such other acts, at the chargee's expense, as may be reasonably required.
viii. That the chargee may distrain for arrears of interest.
ix. That on default of payment of the interest secured by the charge, the principal money shall, at the option of the chargee, become payable.
[...]
Amendment of implied covenants
(3) A covenant deemed to be included in a charge by subsection (1) may, in a schedule to the charge, or in a set of standard charge terms filed under subsection 8 (1) and referred to in the charge by its filing number, be expressly excluded or be varied by setting out the covenant, appropriately amended.
Mortgages Act R.S.O. 1990, CHAPTER M.40
[...]
Covenants to be implied:
7.There shall, in the several cases mentioned in this section, be deemed to be included, and there shall in those several cases be implied, covenants to the effect stated in this section, by the person or by each person who conveys, as far as regards the subject-matter or share thereof expressed to be conveyed by that person or each person with the person, if one, to whom the conveyance is made, or with the persons jointly, if more than one, to whom the conveyance is made as joint tenants, or with each of the persons, if more than one, to whom the conveyance is made as tenants in common, that is to say,
on mortgage by beneficial owner
(a) in a conveyance by way of mortgage, the following covenants by the person who conveys, and is expressed to convey as beneficial owner, namely,
(i) for payment of the mortgage money and interest, and observance in other respects of the proviso in the mortgage,
(ii) for good title,
(iii) for right to convey,
(iv) that, on default, the mortgagee shall have quiet possession of the land, free from all encumbrances,
(v) that the mortgagor will execute such further assurances of the said lands as may be requisite, and
(vi) that the mortgagor has done no act to encumber the land mortgaged
[...]
Prescribed terms
(5) A charge in the prescribed form shall be deemed to include the prescribed standard charge terms, unless a set of standard charge terms filed under subsection 8 (1) is referred to in the charge by its filing number. R.S.O. 1990, c. L.4, s. 7 (5).
Amendment of prescribed terms
(6) A prescribed standard charge term deemed to be included in a charge by subsection (5) may, in a schedule to the charge, be expressly excluded or be varied by setting out the term, appropriately varied. R.S.O. 1990, c. L.4, s. 7 (6).

[179] ROACH, Joseph E., *The Canadian Law of Mortgages*, 2nd ed., Toronto, Butterworths, 2010, p.342
[180] ROACH, Joseph E., *The Canadian Law of Mortgages*, 2nd ed., Toronto, Butterworths, 2010, p.339

Generally, banks and other financial institutions exclude implied covenants and provide their own lists of standard clauses.[181] These clauses are similar to those included in the *Short Forms Acts* of the various provincial jurisdictions.[182] The covenants can still be changed by submitting a new list, but if the charge relates to several lists, only the last list submitted will be considered. The parties may modify or exclude a standard clause included in the charge deed by means of an appendix to the charge that reproduces the modified term. Accordingly, if the parties wish to add future obligations to the charge , there seems to be nothing to stop them doing so. They can negotiate the object and the scope of the mortgage. The important thing is that this clause respects the debtor's inherent right to redeem the legal title and is not contrary to the doctrine of impediments to the right of redemption discussed earlier in this report.

Furthermore, we have observed that some provinces such as Ontario require the holder of the title (the chargee) to provide the constuituent (the chargor) or his solicitor with a list of terms to be included in the charge before the conclusion of the mortgage contract, or be liable to a fine.[183] Many banks now offer mortgage products known as "Multipurpose" mortgages. Also, our own analysis of mortgage contracts has revealed that RBC includes a clause on future obligations in its mortgage contract.[184]

In short, freedom of contract seems to take precedence when it comes to future obligations. Unlike in civil law, where the rules and regulations governing mortgage contracts are included within the same code (the *Civil Code of Québec),* in the common law provinces, the encumbrance can change from one jurisdiction to another and is interpreted on the basis of the legislation from which it arose. Since it may modify and exclude implied covenants included in the legislation, the parties may conclude that the charge can be used to secure future obligations, provided that these are not intended to nullify the debtor's right of redemption or to create collateral benefits for the creditor against the debtor, exposing the latter to excessive and exorbitant obligations that will

[181] The Director of Registration assigns a filing number rating when the list is submitted and send copies identified by their rating, to the land registry offices in the province, within 30 days of submission. All encumbrances registered after filing of a set of standard terms and the assignment of a filing number will be deemed to include all the terms of agreement of this filing number.

[182] Joseph E. Roach, *The Canadian Law of Mortgages*, 2nd ed., Toronto, Butterworths, 2010, p. 243

[183] Land Registration Reform Act, R.S.O. 1990, CHAPTER L.4

8. (1) A person may file with the Director, in the prescribed manner and form, a set of standard charge terms and, with the consent of the Director, may file a set of standard charge terms in a form other than the prescribed form. R.S.O. 1990, c. L.4, s. 8 (1).

Amendment of set of standard charge terms

(2) A set of standard charge terms filed under subsection (1) may be amended by filing a further set of standard charge terms under subsection (1). R.S.O. 1990, c. L.4, s. 8 (2).

[...]

Disclosure: offence

11. A person named as chargee in a charge containing standard charge terms that have been filed under subsection 8 (1) who takes the charge before providing the chargor or the chargor's solicitor with a copy of the standard charge terms is guilty of an offence and on conviction is liable to a fine of not more than $5,000.

[184] Joseph E. Roach, The Canadian Law of Mortgages, 2nd ed., Toronto, Butterworths, 2010, APPENDIX D

result his being prevented from exercising his right of redemption. In short, the parties must respect the debtor's fundamental right to redeem his land.

Regarding disclosure of the extent of the charge by the mortgage lender, only the provinces of Newfoundland-Labrador and British Columbia appear to require the mortgage lender to disclose the extent of the charge .[185] The others are apparently

[185] *Consumer Protection and Business Practices Act*, SNL2009 Ch. C-31.1 (NEWFOUNLAND-LABRADOR)
Disclosure

48. (1) A credit grantor who is required to provide a disclosure statement or a statement of account under this Part shall ensure that the statement

(a) is in writing or another form that is consented to, in writing by the borrower, and the credit grantor shall retain that statement and consent as a record for future use;

(b) contains the information required under this Part; and

(c) expresses that information clearly, concisely, in a logical order and in a manner that is likely to bring the information to the borrower's attention.

(2) A disclosure statement or a statement of account may be a separate document or part of another document provided to the borrower.

(3) Information disclosed under this Part whether in a disclosure statement, advertisement or otherwise may be based on an estimate or assumption if the

(a) disclosure depends on information that is not ascertainable by the credit grantor at the time of the disclosure; and

(b) estimate or assumption is reasonable and is clearly identified in the document effecting the disclosure as an estimate or assumption.

(4) Where an advertisement is published and information is disclosed in that advertisement that, under this Part, requires other information to be included in that advertisement, the credit grantor who publishes or on whose behalf the advertisement is published shall disclose the information in the manner required by regulation.

(5) Where information in a disclosure statement is inconsistent with information or a provision set out in the credit agreement, the credit agreement is presumed to incorporate the information or provision that is more favourable to the borrower, unless it is proven that the less favourable information or provision reflects the borrower's actual understanding of the provisions of the agreement.

Business Practices and Consumer Protection Act, [SBC 2004] CHAPTER 2
Disclosure statements must be given
66 (1) In this section, "business day", in relation to a credit grantor, means a day on which the credit grantor is open for business.
(2) Subject to subsection (3), a credit grantor who has entered into, or who is negotiating to enter into, a credit agreement with a borrower must give the borrower a disclosure statement in relation to the credit agreement before the earlier of
(a) the borrower entering into the credit agreement, and
(b) the borrower making any payment in connection with the credit agreement.
(3) Subject to subsection (4), a credit grantor who has entered into, or who is negotiating to enter into, a credit agreement to provide a mortgage loan to a borrower must give a disclosure statement in relation to the credit agreement to the borrower at least 2 business days before the earlier of
(a) the date on which the borrower incurs any obligation to the credit grantor in connection with the mortgage loan, other than an obligation in respect of an expense referred to in section 57 (2) (e) [value received or to be received by a borrower] or a prescribed expense, and
(b) the date on which the borrower makes any payment to the credit grantor in connection with the mortgage loan, other than a payment in respect of an expense referred to in section 57 (2) (e) [value received or to be received by a borrower] or a prescribed expense.

continuing to adhere to the obligation to disclose the cost of borrowing and the rate set by the *Interest Act* and the cost of borrowing regulations included in their respective legislations.

7.7 Extinction of the mortgage

The mortgage is extinguished when the debtor has fully repaid his debt, as stipulated in the contract.[186] He will then regain title of his land and request to be released from the mortgage. The creditor must reconveyance his legal title: it must not be forgotten that the disposal of the land was made only as security. The parties will complete the form prescribed by the law in force in the province to ensure that the transfer takes place in due form. The registrar will then issue a certificate of discharge, which does not however have the effect of eliminating the rights of the parties to the contract. Thus, if the certificate of discharge is granted for a lesser amount than that recorded in the contract, the creditor may request the correction and the debtor will have to remit the difference.[187]

(4) The borrower under a credit agreement referred to in subsection (3) may waive the time period referred to in that subsection subject to and in accordance with any prescribed terms and conditions.

[186] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 75

[187] Joseph E. Roach, *Les hypothèques immobilières en Common Law*, Cowansville, Les Éditions Yvon Blais, 1991 p. 76

CONCLUSION AND RECOMMENDATIONS

While the mortgage contract can be a useful tool, it is also a complex product. The financial institutions' forms are standardized, and mortgage advisors may have difficulty educating consumers about the extent of their obligations. In Québec, this is the responsibility of the notary.

So what is the problem? The semi-structured interviews we conducted with experts and consumers revealed that the latter are often in a hurry to close the transaction at the notary. Once there, they seem disinclined to listen carefully to details that might prevent them from closing the transaction. In any case, at this stage of the proceedings, it would be very difficult for them to start the whole loan process over again and they could be liable to heavy penalties.

Consumers seem to be poorly informed about their present and future obligations when they enter into such contracts. What is more, they apparently have little choice. Few companies still offer traditional mortgages, even though consumers have told us they would choose this option if they could.

The extent of present and future contractual obligations under the hypothecary loan contract is complex and ambiguous. It is difficult to see what would happen exactly in the case of a mortgage loan contracted with a third party. This is cause for serious concern. Similarly, according to the experts interviewed, lenders seem more inclined to give a discharge from the mortgage than a complete write-off when the principal loan is repaid. Therefore, consumers might have difficulty changing financial institutions or liberating themselves from their mortgage when they sell their home. They may also have to repay all loans covered by the mortgage before they can be fully released.

RECOMMENDATIONS

In the light of the above findings, Option consommateurs recommends:

CONSUMERS

To inform themselves about the type of mortgage proposed by the financial institution and to read it carefully before signing the agreement with the notary.

Whenever possible, to avoid taking out other loans from the financial institution to ensure that all their new debts are not secured by the mortgage on their home, unless that is their wish.

FINANCIAL INSTITUTIONS

To publish information on their websites about the present and future obligations of borrowers covered by mortgages and to ensure that consumers can easily access this information.

To ensure that their employees are able to inform clients about the type of obligations attached to the mortgage and provide them with the appropriate training.

To adjust the terms of each loan secured by the mortgage in accordance with this security, including interest rates on credit cards.

To simplify the terms of hypothecary loan contracts.

To grant an extinction of the mortgage once the loan principal is repaid in full.

THE GOVERNMENT OF QUÉBEC

To amend its legislation to require financial institutions to adjust the terms of each loan secured by the mortgage in terms of this security, including interest rates on credit cards, unless the financial institutions agree to do so voluntarily.

Option consommateurs supports the position of the Chambre des notaires du Québec and requests that the Government prohibit the mortgage from extending automatically to new obligations, unless the consumer or the new owner of the property consents to their property being used to secure these new obligations.

THE GOVERNMENT OF CANADA

To amend its legislation to require financial institutions to adjust the terms of each loan secured by the mortgage in accordance with this security, including interest rates on credit cards, unless the financial institutions agree to do so voluntarily.

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http://www.rbcroyalbank.com/personal.html

8. List of Appendices

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8.1 APPENDIX A – Definitions of the hypothecary loan contract

DESJARDINS GROUP

http://www.desjardins.com/en/particuliers/produits_services/financement/hypothecaire/marge_atout.jsp

Consulted: July 13, 2011

No explanation or definition given of the hypothecary loan contract. The website refers to "Versatile Line of Credit" (a line of credit secured by a mortgage) and the "Multiproject Option" (refinancing).

SCOTIABANK

http://www.scotiabank.com/ca/common/pdf/mortgage/personal_credit_agreement_companion_booklet1151010.pdf

Consulted: July 13, 2011

No definition given of the hypothecary loan contract. The booklet gives information on the Scotiabank "Total Equity Plan," which it refers to as a form of "Collateral Mortgage."

CIBC BANK

https://www.cibc.com/ca/loans/loans-glossary.html

Consulted: July 13, 2011

Definitions

Security (Lending): Property, either real estate or an investment product, pledged as collateral for a loan or line of credit to help the borrower obtain a lower interest rate and a higher borrowing limit from the lender.

Home equity line of credit: A secured line of credit borrowed against the equity in your home. Funds are borrowed once, but can be accessed any time, up to the limit specified. The credit limit is usually larger than other forms of unsecured borrowing.

Secured Loan: A loan may be fully or partially secured by real estate or other property or investments which have a realizable value at least equivalent to the amount of the loan taken.

CIBC offers information on a line of credit and the CIBC "Home Power Mortgage." To be eligible for the latter product, the website states that "mortgage applicants must meet CIBC lending criteria."

TD BANK

https://www.tdcanadatrust.com/products-services/banking/index-banking.jsp

Consulted: July 13, 2011

No definition given of the hypothecary loan contract.

TD Bank has two products, the "Home Equity Line of Credit" and the "Green Home Equity Line of Credit," which allow consumers to use the value of their home to borrow money. Both products are found under the "Mortgages" tab. However, there is no mention anywhere that this is a hypothecary loan contract.

Under the tab Apply> Before you begin> Useful Information>Remarks: It was mentioned for the first time there will be a fee assessment to determine the value of the residence and legal fees for the registration of mortgage used as security in the case of a credit line or home mortgage.

It was also mentioned that a co-owner of the house must be on the application as a co-borrower or co-applicant and must sign the loan agreement.

NATIONAL BANK

http://www.bnc.ca/bnc/cda/index/0,4229,divId-2_langId-2_navCode-1000,00.html

Consulted: July 13, 2011

No definition given of the hypothecary loan contract.

Definition of Mortgage line of credit: Line of credit that is secured by a mortgage.

The product "Revolving Clause" permits the consumer to borrow back, at any time, unused principal up to the amount of the registered loan.

The product "All-In -One-Banking" is a line of credit secured by a mortgage. This is not made clear, however, on the website, where it talks about it being a tool that makes it possible to get financing of up to 80% of the value of one's home.

LAURENTIAN BANK

https://www.banquelaurentienne.ca/en/personal_banking_services/index.html

Consulted: July 13, 2011

No definition given of the hypothecary loan contract.

The website presents the "Homeowner's Kit," which may include several mortgage financing products and/or a home equity line of credit. It also states that all one's debts can be consolidated "under one roof." There is no mention that this is in fact a hypothecary loan contract; merely that it is a "mortgage financing tool."

BANK OF MONTREAL

http://www.bmo.com/home?nav=top

Consulted: July 13, 2011

Under the tab: Personal> Personal Banking>Tap into your home equity

The website presents the product "Homeowner's Line of Credit," which offers a line of credit of up to 80% of the value of the home; this is secured by the home or by other real estate.

The Homeowner Line of Credit replaces the traditional mortgage. Consumers are informed that a credit application is sufficient to finance up to 80% of the current value of their home. The money already paid back on the credit line automatically becomes available. They can access funds up to the credit limit as often as they wish.

The Homeowner Line of Credit is secured against the consumer's home, but gives immediate access to the authorized credit limit, minus any outstanding loans or mortgages.

The BMO Mortgage Glossary (http://www.bmo.com/home/popups/personal/mortgage-glossary/), gives the following definition:

Collateral mortgage: A loan evidenced by a promissory note and backed by the collateral security of a mortgage on a property. The money borrowed is generally used for a purpose other than the purchase of a home, such as a vacation or home renovations.

ROYAL BANK

http://www.rbcroyal bank.com/

Consulted: July 13, 2011

Definition: Line of Credit

A type of credit which offers an individual immediate access to any portion or all of a pre-determined amount of cash upon demand. A line of credit may be either unsecured or secured with personal assets such as bonds, term deposits or equity on a home. A secured line of credit results in lower risk to the financial institution and a lower rate of interest to the individual

The website present the product “Royal Credit Line” (Secured Line of Credit option) that allows consumers to can use the equity in their your homes or investment portfolio as collateral to secure a higher credit limit at a lower interest rate..

Another product is the RBC Homeline Plan, which combines the mortgage and personal credit under one plan. It is not made clear that this is a hypothecary loan contract.

8.2 APPENDIX B - Questions for semi-directed interviews

Have you ever taken out a mortgage? When? Was it your first mortgage?

If not, how many mortgages have you subscribed to?

When you took out the loan, what you were told?

Did the mortgage advisor offer you a choice of formulas (traditional loan, line of credit mortgage, hypothecary loan contract)?

If so, what were they?

Did the mortgage advisor present you with a contract?

If so, did you read the contract before signing it?

Were there any parts that surprised you?

If so, which ones?

When purchasing a mortgage, did you also want to have money to do other things (renovation, line of credit, car loan)?

Could the product you were offered cover other loans?

If so, did your mortgage advisor explain the advantages of such a formula?

Did your advisor explain the disadvantages of such a formula?

Did your notary explain the advantages of such a formula?

Did your notary explain the disadvantages of such a formula?

Were there some parts that you did not read when you were with your mortgage advisor?

What do you think of the hypothecary loan contract?

Would you recommend this formula?

Would you discourage someone from choosing it?

8.3 APPENDIX C - Focus Group Report on Hypothecary Loan Contracts (Umbrella Mortgages)

[See French Report for this appendix.]

8.4 APPENDIX D – Hypothecary Loan Contracts – Discussion Guide

[See French Report for this appendix.]