

Hendrix Law

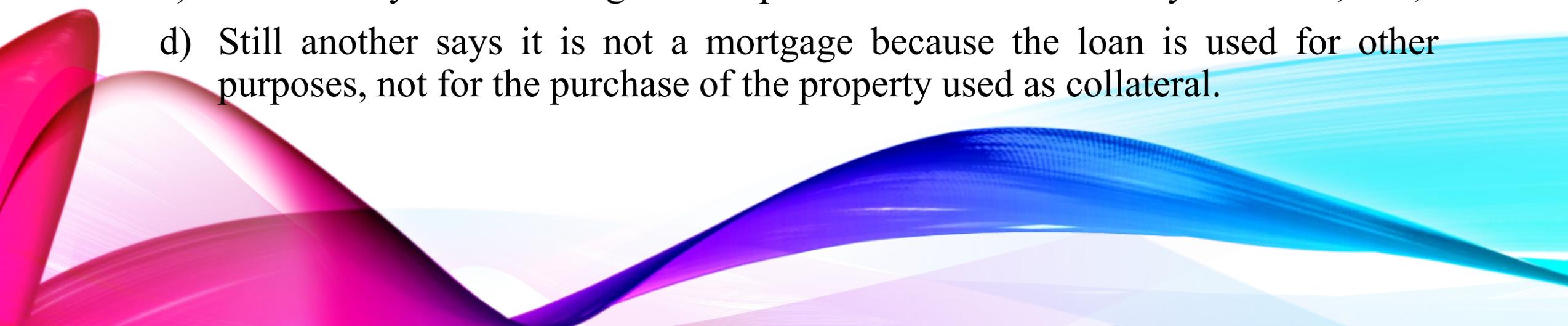
COLLATERAL MORTGAGES IN ALBERTA

Presented by Hendrix Law



Does anyone Really know what a Collateral Mortgage is?

If you do a search on Google you get all kinds of answers:

- a) Several say that is it a charge that is registered at Personal Property Registry only;
 - b) Another says it is both a promissory note and security in the form of a lien registered against the property;
 - c) Another says it can be registered up to 125% of the value of your home, and;
 - d) Still another says it is not a mortgage because the loan is used for other purposes, not for the purchase of the property used as collateral.
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The true definition of a Collateral Mortgage:

- The Courts in Alberta have always looked at Collateral mortgages as mortgages granted collateral or subsidiary to other series of loans or debt obligations which fall as an exception to Section 40(1) of the *Law of Property Act* which provides as follows:
 - “In an action brought on a mortgage of Land, whether legal or equitable, or on an agreement for sale of the Land, the right of the Mortgagee or vendor is restrict to the Land to which the mortgage or agreement relates and to foreclosure of the mortgage or cancellation of the agreement for sale, as the case may be, **and no action lies**
 - (a) on a covenant contained in the mortgage or agreement for sale.”

Section 43 of the *Law of Property Act*, provides that Section 40 does not apply to (subsection 1) mortgages given by a corporation or (subsection 4) mortgages given to secure a loan under the *National Housing Act (Canada)* or (subsection 4.1) high-ratio mortgages insured by an insurer under the *Insurance Act*.

Currently, only CMHC is insured under the *National Housing Act (Canada)* and Genworth and Canada Guaranty are insured under the *Insurance Act*.

While not critical, to avoid the covenant the mortgage is required under the regulations of the *Law of Property Act* to contains the following wording:

This Mortgage is a High Ration Mortgage to which Sections 43(4.1) and (4.2) and 44(4.1) AND (4.2) of *The Law of Property Act* apply. You and anyone from you who, expressly or impliedly assumes this Mortgage from you, could be sued for any Obligations under this Mortgage if there is a default by you or by a person who assumes this Mortgage.



- We think of a Collateral mortgage as a way behind the “Law of Property Act” restricting the ability of the Lender to collect on a personal covenant to pay on a mortgage. To do this, there must be the following pre-requisitions (*Royal Bank of Canada v. Stallman, 2009, ABQB 766*):
 - A pre-existing basket of securities that the Lender needed shoring up by a mortgage;
 - A consolidation of existing debt concurrent with the granting of additional security;
 - An increase in the indebtedness concurrent with the granting of additional security to add to the existing security;
 - Generally this increase in security is done when the loan is in default;
 - And the value of the land would not be sufficient to pay the debt in full, and;
 - The Lender is generally looking at the borrower’s ability to pay as the primary security for their loan

In the last 10 years, banks have been speaking of collateral mortgages by referencing them as “Homeline Plans, Matrix mortgages, Home Product Plans, Integrated mortgages, etc.

Currently, right now there is a growing trend with major banks to register a mortgage for an amount more than the actual sum being advanced on the purchase of a property or a refinancing of that property. They are sometimes also being registered for an interest rate higher than was agreed to by the parties at the time of the mortgage commitment.

That excess amount registered can either be subsequently advanced or used as security for additional credit provided to the borrowers.



What a new Collateral Mortgage does for the Borrowers:

The additional amounts being registered on title with the higher interest rates, allow the Borrower to

- a) lock in a variable rate mortgage at amount no higher than the registered sum;
- b) Obtain additional financing secured by the mortgage without having to re-attend with a lawyer to sign additional security documentation;
- c) More easily be qualified for additional credit that would be secured on the mortgage when equity is built up in the property;
- d) Look first to that Lender for future borrowings as the security is already in place.
- e) Saves fees and legal costs to do a refinance.
- f) In some cases, provides access to a line of credit in circumstance where they may not otherwise qualify for one!

What a new Collateral Mortgage does for the Lender:

The additional amount and higher rate on this new form of Mortgage allows the Lender to:

- a) Have an already secured customer for new security for loans, credits cards and lines of credit;
- b) Have a fast closing with new security for the Borrower;
- c) Be able to advance new funds under the Mortgage without re-registering and just adding the new credit facility to the existing Mortgage;
- d) Add credit card, over draft and other security to a mortgage foreclosure action to collect against the land
- e) Have increased flexibility on their borrowing arrangement with pre-existing security registration



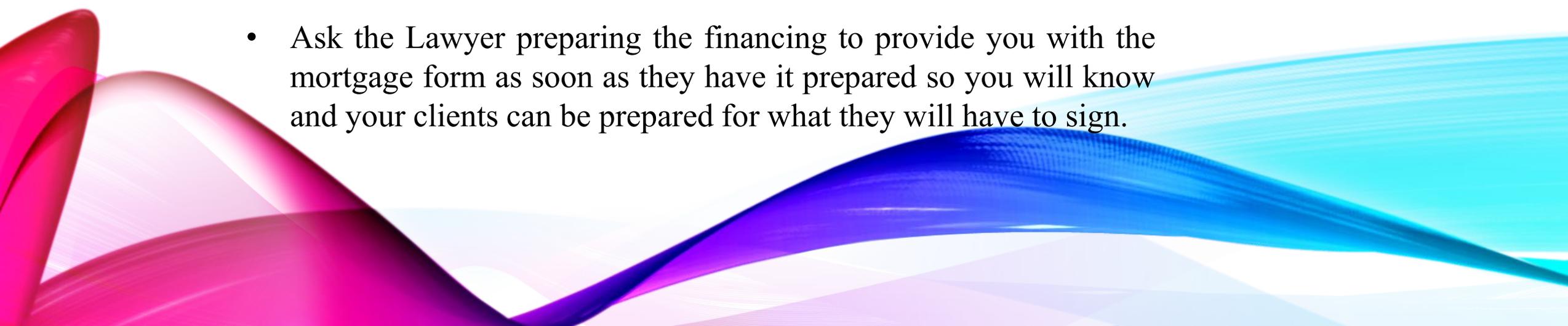
How is this impacting private or second mortgage Lenders?

- It requires the Borrower to go to the original Lender to see if they can get additional money from them before exploring that possibility with anyone else
- The Lender may not offer the Borrower the option of obtaining a fixed rate mortgage for a fixed amount payable over an amortized period of time.
- Mortgages are often registered for more than the sum advanced and you may or may not be able to tell on the face of the mortgage, if the mortgage itself is re-advancable
- If the mortgage is not re-advancable at the time of the second mortgage, it does not prevent the first Mortgagee from advancing up to their registered principal sum at any time in the future
- Lenders won't approve financing behind these mortgage registered for more than has been advanced.

How is this impacting Borrowers?

- Borrowers go to signings with their Lawyers and are shocked and surprised to see Mortgage documents that don't reflect their mortgage commitments.
- Borrowers are getting confused about how much equity they have in their homes.
- While they may be already secured for additional funds, Lenders may not be willing to provide the Borrowers will additional credit facilities secured by that Mortgage
- If the Lender is willing to provide additional credit facilities, there is no pre-agreement as to rate or terms for that future advance and the Borrower may be able to get a better rate or terms from a different Lender
- Prepayment penalties still apply to the advanced portion of the registered mortgage
- Borrowers may not remember from their original signing of their mortgage form the ability of the Lender to add any unsecured debt to the mortgage balance.
- Borrowers need to be aware that if they default under other security to the Lender, the Lender may be able to foreclose!

What is the solution? Re: Brokers

- I think the first thing is we need to do is have our Brokers ask, when they are qualifying a Borrower for a mortgage, if the mortgage being instructed to the Lawyer for the Purchaser/Borrower is going to be for more than was advanced and for a higher interest rate than set out in the mortgage commitment.
 - Secondly, if the Lender offers a strict mortgage for only the sum advanced, if they will instruct under that method
 - We need to advise our Borrowers that they may be able to insist on a fixed rate, fixed interest rate mortgage in accordance with their mortgage commitment.
 - We ALL need to read the FINE PRINT (fine print!!)
 - There is a legislated process in Alberta to have a mortgage which is registered for more than the funds advanced to be reduced to the Principal sum owing at any time.
 - Ask the Lawyer preparing the financing to provide you with the mortgage form as soon as they have it prepared so you will know and your clients can be prepared for what they will have to sign.
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What is the Solution? Re: Private Lenders

Some websites suggest that you are stuck with the Lender who is registered for more than the funds have been advanced, when they refuse to advance you further funds. For example, they are registered for \$750,000.00 but have only advanced \$500,000.00 and refuse to then advance the other \$250,000.00

NO ONE is TIED TO A LENDER FOREVER!!

Private Lenders must note that generally speaking a re-advanceable mortgage is not transferrable to a Third Party, so they can not pay out the credit facilities associated with the Mortgage on title without offering the same credit facilities.

However, this does not mean that the Collateral Mortgage can not be discharged! Even if the mortgage form does not show a maturity date, the Borrower is entitled to rely upon the terms and conditions of the supporting mortgage documentation for their pre-payment terms on the fixed portion of their mortgage.

What do we do?

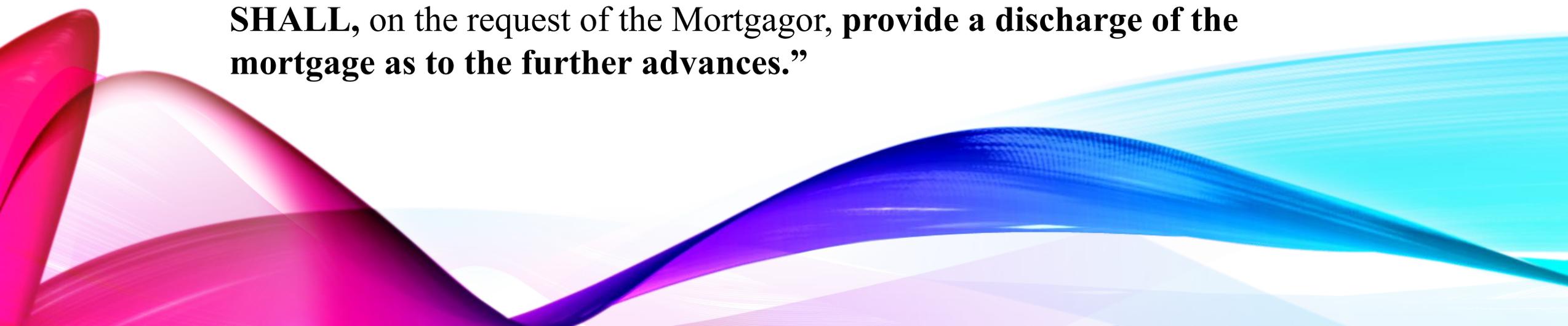
Section 104 (1) of the Land Titles Act states:

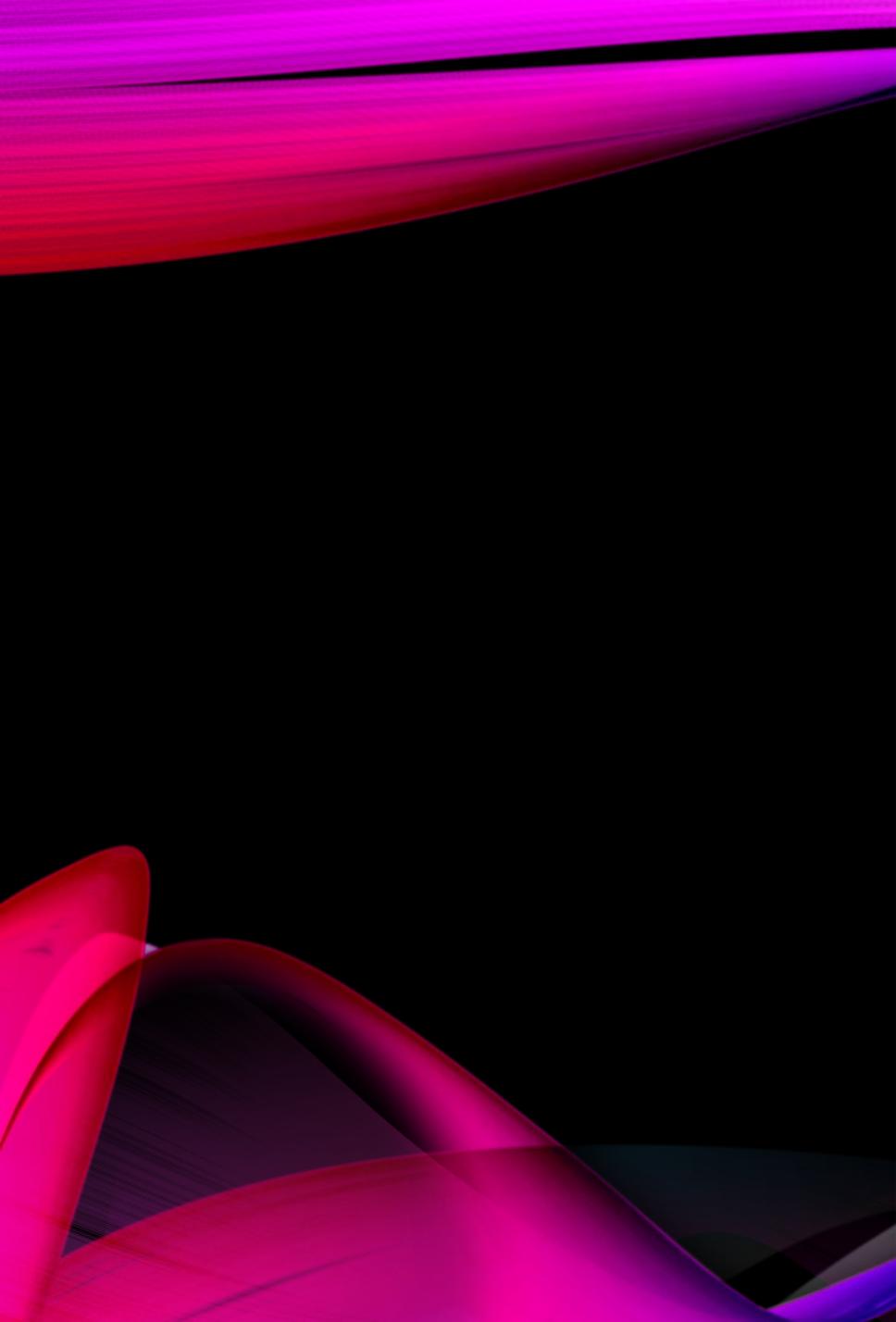
“ On registration of a mortgage for a specific principal sum, the mortgage obtains priority in accordance with section 14 of this Act for all advances and obligations secured pursuant to the terms of the mortgage, notwithstanding that they are made or incurred subsequent to the registration,.. of any other instrument or caveat.”

Subsection (3) then states:

“If a Mortgagee refuses to make, or a mortgagor has and exercises a right to refuse to accept or be bound by, any further advances that would be secured under subsection (1) or (2), the Mortgagee

SHALL, on the request of the Mortgagor, provide a discharge of the mortgage as to the further advances.”





What is unusual about this provision of the *Land Titles Act* is that it puts a positive duty upon the Lender to provide to the Borrower a partial discharge of the mortgage for the un-advanced portion of the mortgage.

The Borrower **DOES NOT** have to ask the Lender to advance the balance and be refused. If the Borrower says he refuses to be **Bound By** any further advances secured by that mortgage, the Lender **SHALL** discharge the mortgage to the portion unadvanced.

The other alternative is for the Borrower to request the further advance and be denied, then the Lender again, **SHALL** discharge the mortgage to the portion unadvanced.

SO,

Firstly, we have to have either a request for the additional money and have that money refused, or a direction to the Lender that the Mortgagor refuses to be bound by any further advances.

Secondly, we have to request and direct the Lender to provide the partial discharge of the Mortgage as to any un-advanced portion of the Mortgage.

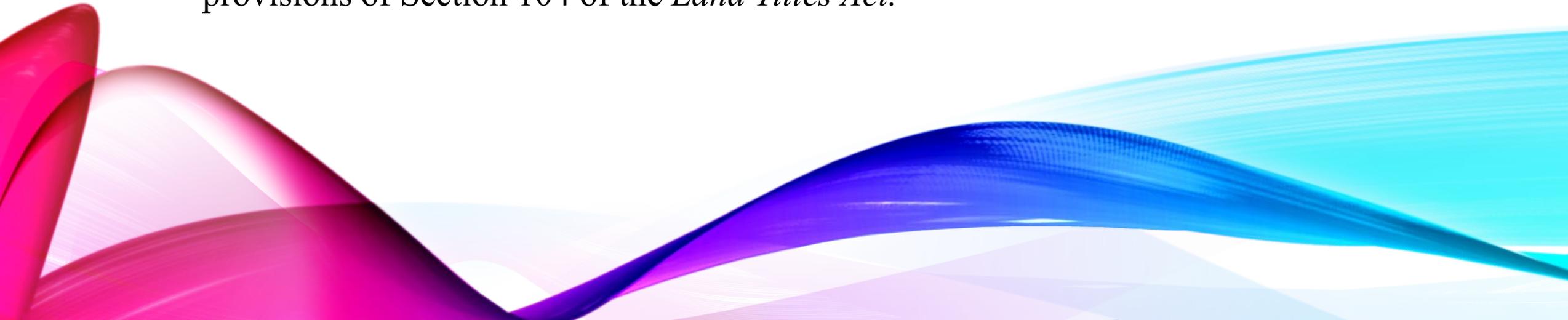


Now, this is all well and good, but the practical reality is:

- Existing Lenders may actually advance further under their mortgages if funds are requested or the demand is made for a partial discharge and you can lose the deal, or;
- the Borrower is not willing to make the effort with the current Lender to get a signed acknowledgement not to re-advance or a partial discharge of the mortgage, or;
- You may not be willing to wait on the deal for the actual partial discharge of the mortgage before you can make use of your funds elsewhere.

So, how do we deal with it:

- 1) We have the borrowers sign an Irrevocable and Unconditional Direction not to Re-Advance on the registered mortgage and take it to the Lender to have it signed by them before you commit to a mortgage transaction.
- 2) We have the borrowers sign an Irrevocable and Unconditional Direction not to Re-Advance and serve it formally on the Lender with the direction to comply with the provisions of Section 104 of the *Land Titles Act*.





While the provisions of the *Land Titles Act*, specifically provides that a Mortgagor has the right to refuse to be bound by any further advance and upon that refusal, they can request and the Lender **SHALL** discharge the mortgage as to those further advances, we do have concerns about the possible legal argument that a contract can not be unilaterally amended by one party.

In my opinion, the best course of action is to provide the notice to the Lender and have it acknowledged by the Lender that your Borrower is requesting the partial discharge, to know that you have the necessary priority under the *Land Titles Act*.

This process has not been challenged under the Court system to date. So currently we have no case precedent to confirm the priority of any subsequent charge when the request is made to the prior mortgagee for the partial discharge.

We maintain that the legislation is clear and unequivocal on its face and therefore has to be strictly interpreted to require the partial discharge.

ANY QUESTIONS?



Hendrix Law

**THANK YOU
FOR TAKING
THE TIME
WITH ME
THIS
AFTERNOON!**

We are always ready, willing and able to assist you on any mortgage transactions or enforcements