CONSUMER ADVISORY PANEL

April 26, 2023

Delivered electronically

Financial Services Regulatory Authority of Ontario
25 Sheppard Ave W, Suite 100
Toronto, ON
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Re: Proposed Guidance: Detecting and Preventing Mortgage Fraud

The Consumer Advisory Panel (CAP) welcome this opportunity to comment on Proposed Guidance: Detecting and Preventing Mortgage Fraud. Given the current mortgage environment characterized by a combination of high housing costs and elevated interest rates, we believe that the Proposed Guidance is both timely and necessary. We, therefore, commend FSRA for pursuing this important matter and would like to take this opportunity to put forward recommendations designed to reinforce the consumer protection provisions in the Proposed Guidance to detect and prevent mortgage fraud.

The Proposed Guidance have been designed to address the limitations of the current regulatory and ethical framework governing mortgage brokers. From a consumer perspective, we applaud FSRA's intent, however, we are not convinced that the Proposed Guidance will adequately protect consumers from experiencing mortgage fraud. We are concerned that the Proposed Guidance relies too heavily on Codes of Conduct and disclosure as the primary means for deterring mortgage fraud.

While Codes of Conduct can provide guidance and establish standards of conduct for mortgage brokers, they are limited as a means of consumer protection:

- Lack of enforceability: A code of conduct is typically not legally binding and may not have effective enforcement mechanisms, meaning that there may be little recourse for consumers if the code is not followed.

- Conflicts of interest: A code of conduct may not be effective in preventing conflicts of interest, as brokers may prioritize their own interests over those of their clients.

- Limited scope: A code of conduct may not address all of the potential risks and harms that consumers may face in the mortgage broking sector, particularly as the industry evolves and new risks emerge.

- Lack of consumer input: A code of conduct is often developed without sufficient input from consumer advocates or other stakeholders, leading to potential blind spots or oversights.

Therefore, while Codes of Conduct can be a useful tool for establishing standards of conduct and promoting ethical behavior, they should not be relied upon as a primary means of consumer protection. Additional measures, such as comprehensive regulation and oversight, consumer education, and effective enforcement mechanisms, are also necessary to protect consumers and prevent fraud in the mortgage broking sector.

Disclosure is the other key element identified in the Proposed Guidance in the fight against conflicts of interest and fraudulent practices in the mortgage broking industry. However, disclosure on its own is an imperfect technique to protect consumers from the risks associated with mortgage fraud.

- Inadequate comprehension: Many consumers may not fully understand the disclosure statements or the implications of the conflicts of interest that are disclosed.

- Power imbalance: Consumers may feel pressured to agree to the terms of a mortgage, even if there are potential conflicts of interest or other risks, due to the power imbalance between them and the mortgage professional.

- Insufficient information: Disclosure may not provide consumers with enough information to make informed decisions, particularly if the disclosures are buried in fine print or written in complex legal language.

- Limited effectiveness: Even if consumers understand the disclosures and the potential risks, they may not have sufficient bargaining power to negotiate better terms or find an alternative mortgage professional.

In addition, behavioral economics has identified other limitations when relying on disclosure to protect consumers:

- Confirmation bias: Consumers may be more likely to focus on the positive aspects of a mortgage offer and overlook the potential risks or conflicts of interest, due to their own confirmation biases.

- Complexity bias: Consumers may be less likely to fully comprehend complex disclosures, leading them to make suboptimal decisions.

- Loss aversion: Consumers may be reluctant to switch mortgage professionals even if they are aware of potential conflicts of interest or risks, due to the fear of losing out on a good deal or the hassle of starting the process over again.

- Trust bias: Consumers may overestimate the trustworthiness of mortgage professionals, leading them to ignore or downplay potential conflicts of interest or risks.

Given these limitations and given the inherently conflicted nature of mortgage broking[1], CAP recommends that the Proposed Guidance supplement Codes of Conduct disclosure and with additional mitigants designed to protect consumers, including:

- Prescribing the type of information brokers must provide prospective consumers about any incentives or commissions they receive from lenders for recommending certain loans.

- Setting out minimum standards of conduct that every broker must observe and maintain.

- Establishing a best interest standard for mortgage brokers.

It is our view that by incorporating these initiatives in the Proposed Guidance, FSRA can help to meaningfully reduce fraud in the mortgage broking area and improve consumer protection in Ontario.

If you require additional information or any clarification, please let us know.

Sincerely,

Consumer Advisory Panel

[1] Conflicts of Interest in the Mortgage Industry: Implications for Consumer Protection and Housing Policy" by Patricia A. McCoy and Susan Wachter, published in the Journal of Real Estate Finance and Economics in 2009