



Financial Services
Commission
of Ontario

Report on FSCO's Compliance Reviews of Mortgage Brokerages 2010-2014

Financial Services Commission of Ontario
Licensing and Market Conduct Division
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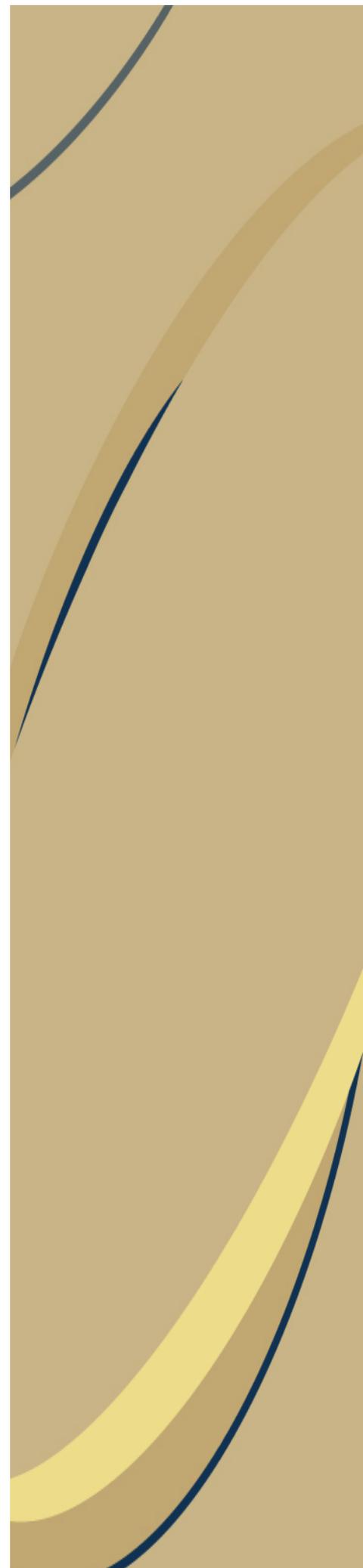


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Executive Summary

Since the introduction of the Mortgage Brokerages, Lenders and Administrators Act, 2006 (MBLAA) that went into effect on July 1, 2008, and several new regulations on standards of practice that went into effect on January 1, 2009, the Financial Services Commission of Ontario (FSCO) has conducted a series of on-site examinations of mortgage brokerages to ensure consumer protection. Upon completion of each examination cycle, FSCO identified the trending issues and/or deficiencies in the brokerages' operations that needed to be addressed. This report summarizes the results of examinations conducted from 2010 to 2014.

Based on the analysis of all the examinations conducted in the period from 2010-2014, the overall results demonstrate that the majority of mortgage brokerages understand the requirements of the legislation and FSCO's expectations for brokerages to have complete policies and procedures to govern their day-to-day compliance with the legislation.

It is however noted that brokerages still need to make improvements to their policies and procedures in certain areas, such as providing adequate disclosures to borrowers and investors/lenders, and including the required information on public relations materials.

The results from the examinations continue to support FSCO's risk-based approach to regulation and its positive impact on the mortgage brokering industry in promoting higher standards of practice, and in advocating consumer protection in Ontario.

About the Financial Services Commission of Ontario

The Financial Services Commission of Ontario (FSCO) is an agency of Ontario's Ministry of Finance that is responsible for regulating mortgage brokerages, administrators, brokers and agents in Ontario. FSCO is also responsible for overseeing other financial services sectors, including insurance, pension plans, loan and trust companies, co-operative corporations, credit unions and caisses populaires and service providers who invoice automobile insurers for statutory accident benefits claims in Ontario.

The Commission's legislative mandate is to provide regulatory services that protect the public interest and enhance public confidence in the sectors it regulates. As an organization, FSCO is committed to being a progressive and fair regulator supporting competitive financial services sectors.

FSCO uses a risk-based approach to regulation that focuses on allocating valuable regulatory resources to those areas that are deemed to have the highest risk. The benefit of this approach is that regulatory resources are maximized and compliance costs are minimized. The Compliance Reviews provide one source of information to support this risk-based approach.

Introduction

In 2009 FSCO began to conduct annual on-site examinations of mortgage brokerages to determine the extent to which they had prepared themselves to meet their legal obligations under the MBLAA. These examinations assessed the degree to which brokerages had established and implemented policies and procedures reasonably designed to ensure compliance with the requirements under the MBLAA.

The findings from FSCO's reviews indicated that most mortgage brokerages had established policies and procedures in accordance with the regulations. However, the quality of those policies and procedures was not sufficient to mitigate the risk of non-compliance with the law and the potential for harm to consumers.

As a result, between 2010 and 2014, FSCO continued to conduct mortgage brokerage examinations on both a random and targeted basis. These examinations assessed whether the brokerages' policies and procedures were sufficient for the nature, complexity and size of the brokerage and if the requirements prescribed in these policies and procedures were followed.

In addition, the examinations verified whether the principal brokers were adequately supervising the brokerages. FSCO's risk-based approach to regulating the mortgage broker industry does not include oversight of the day-to-day activities of brokers and agents. The onus rests with the principal broker to adequately supervise all brokers and agents that are authorized to deal and trade in mortgages within that brokerage.

This report summarizes the results of the examinations over the five year period. The report also sets out FSCO's expectations of licensed brokerages with respect to compliance with MBLAA and its regulations and the consequences for brokerages if they are found to contravene the law.

Review Methodology

Over the past five years, FSCO has examined almost half of licensed mortgage brokerages in Ontario. Below is an overview of the number of brokerages examined on an annual basis. In some cases, follow up examinations were conducted to verify that prior recommendations had been actioned. These follow up examinations were infrequent, and would account for under 10 per cent of mortgage brokerages examined.

Figure 1 – Number of Brokerages Examined, 2010-2014

Year	Number Of Brokerages Examined	Percentage Of Licensed Brokerages Examined
2010	122	10%
2011	74	6%
2012	50	4%
2013	141	12%
2014	184	15%
Total	571	47%

The main objective of the reviews was to verify that brokerages demonstrated overall compliance with the MBLAA and that as a result, consumer protections were in place. More specifically, the reviews were conducted to ensure:

- That policies and procedures were in place and were sufficient for the nature, complexity and size of the brokerage
- There was adequate supervision of the brokerage, brokers and agents, and
- That adequate disclosures were made to borrowers and investors/lenders.

Following each examination, findings and recommendations were reviewed with the principal broker, along with an overview of any identified deficiencies. These recommendations emphasized FSCO's expectations of the mortgage brokering industry, and encourage participants to operate at a level above the minimums which are set out in the MBLAA.

In instances where FSCO identified violations of the MBLAA and related regulations during the examinations, these findings were promptly brought to the attention of the principal broker, and required immediate action to be taken by the brokerage to achieve compliance. In those cases where violations were deemed a high risk for potential public harm, the mortgage brokerages were referred for further regulatory action, including Administrative Monetary Penalties (AMP).

The risk-rating methodology was applied consistently throughout the 2010-2014 examinations. The examination findings were given a rating of low, medium or high according to the following risk-rating definitions:

-  Low risk – 90 per cent or more of brokerages demonstrated a good level of compliance with the requirements noted in the given section.
-  Medium risk – between 80 and 90 per cent of brokerages demonstrated a good level of compliance with the requirements noted in the given section.
-  High risk – less than 80 per cent of brokerages demonstrated a good level of compliance with the requirements noted in the given section.

Findings

The following is a breakdown of the level of compliance observed over the last five years in the thirteen sections of the examination program:

1. General Requirements

FSCO examined whether there are policies and procedures describing the disclosure requirements that the brokerage and its authorized brokers and agents are required to follow when advertising and/or distributing public relations materials.

Over the past five years, FSCO has observed a steady decline in the level of compliance with this section. FSCO found that the brokerage license number and/or legal or trade name was often not disclosed. Other noted violations included brokerages advertising false or misleading information and the address of the brokerage being inconsistent with the information provided to FSCO.

While the number of examinations between 2013 and 2014 increased, partially accounting for the examination findings, there was no correlation noted with the size of the brokerage. The level of compliance with the general requirements is unacceptable and FSCO will be assessing a further regulatory response to change these behaviours.

Figure 2 – Compliance with General Requirements

Year	2010	2011	2012	2013	2014
Risk Rating					

2. Duty to Supervise Brokers and Agents

FSCO examined whether mortgage brokerages have in place the required policies and procedures to supervise brokers and agents and ensure they are complying with practice standards such as: verifying the identity of borrowers, lenders and investors; determining the suitability of a mortgage or mortgage investment for a borrower, lender or investor; identifying and disclosing material risks to borrowers, lenders and investors; identifying and disclosing potential conflicts of interest; and, whether brokers and agents are receiving incentives other than money from other persons and entities.

FSCO observed a consistent level of compliance with this section as the mortgage brokerages made the most up-to-date policies and procedures available for all agents and brokers.

However, FSCO identified a number of deficiencies when it conducted a random sampling of mortgage transactions completed within the preceding 12 months. Specifically the file reviews revealed: poorly documented or lack of disclosure documentation with regards to the suitability of a mortgage product or investment; non-disclosure of material risks or conflicts of interest; minimum wait times not being met; and, a lack of disclosure to the investor/lender regarding the borrower's existing mortgage defaults in the preceding 12 months.

There has been a significant decline in compliance in these areas year-over-year. The lack of proper consumer disclosure and due diligence around product suitability is a high risk area.

FSCO expects mortgage brokerages to actively supervise their agents and brokers to ensure compliance with all of the disclosure requirements. FSCO is currently assessing its regulatory response to correct for this type of contravention.

Figure 3 – Duty to Supervise Brokers and Agents

Year	2010	2011	2012	2013	2014
Risk Rating					

3. Syndicated Mortgages

Brokerages that syndicate mortgages must have provisions in their policies and procedures to govern syndicated mortgages in areas such as disclosure, supporting documentation and time periods for providing information to borrowers and investors/lenders. These provisions relate to Ontario Regulation 188/08, s. 3, 24 (1), 26 (3), 27, 31, 36.

FSCO observed a rise in the level of compliance with this section, due mainly to brokerages having established policies and procedures and documentation to support syndicated mortgage transactions. Given the significant risk syndicated mortgage investments pose to consumers, FSCO will be conducting a more detailed examination of these transactions over the next year.

Figure 4 – Compliance with Syndicated Mortgages Policies and Procedures

Year	2010	2011	2012	2013	2014
Risk Rating					

4. Duty to Establish a Complaints Process

FSCO examined whether brokerages have a complaint handling process as required under Ontario Regulation 188/08, s. 41. As part of this review FSCO considered: whether the brokerage has an established process for complaints resolution; whether an individual has been designated as the complaints officer; and, whether the brokerage retains a complaints log that tracks complaints from the public and that includes the brokerage’s written responses.

Overall, brokerages demonstrated a consistent level of compliance with this section. In some cases however, FSCO did find that improvement could be made by including provisions in the policies and procedures to keep a record of all written complaints received from the public and all written responses to the complaints from the brokerage, as a best practice.

Figure 5 – Compliance with Duty to Establish a Complaints Process

Year	2010	2011	2012	2013	2014
Risk Rating					

5. Duty to Have Insurance

Within this section FSCO verified whether mortgage brokerages had a valid errors and omissions insurance policy as per Ontario Regulation 188/08, s. 42. The law requires a brokerage to have valid coverage at all times while it is licensed. FSCO immediately commences regulatory action (i.e. license suspension, revocation and/or AMP) if the findings reveal that a brokerage does not hold the required insurance coverage.

Overall, this section is rated low risk, indicating a good level of compliance was consistently observed between 2010 and 2014.

Figure 6 – Compliance with Duty to Have Insurance

Year	2010	2011	2012	2013	2014
Risk Rating					

6. Duty Regarding Authorization of Brokers and Agents

FSCO examined whether mortgage brokerages' policies and procedures included provisions for determining if an individual is eligible to be licensed as a mortgage broker or agent as per Ontario Regulation 188/08, s. 43.

FSCO observed an improvement in this section, as mortgage brokerages have begun to amend their policies and procedures to include business practices regarding the termination of a broker's or agent's access to their software provider when no longer authorized by the brokerage, and to notify the Superintendent of any broker or agent that is not suitable to be licensed.

Figure 7 – Compliance with Duty Regarding Authorization of Brokers and Agents

Year	2010	2011	2012	2013	2014
Risk Rating					

7. Restrictions on Payments by the Brokerage

Within this section FSCO verified whether mortgage brokerages provided payments or other remuneration to brokers or agents registered at another brokerage or an unlicensed individual as stated in Ontario Regulation 188/08, s. 44.

FSCO observed an increase in compliance indicating that the brokerages' policies and procedures and business practices included restrictions on payments to unlicensed entities and individuals.

Figure 8 – Compliance with Restrictions on Payments by the Brokerage

Year	2010	2011	2012	2013	2014
Risk Rating					

8. Payments of Incentives Other Than Money

FSCO reviewed whether mortgage brokerages provided any incentives, other than money, to brokers or agents registered with another brokerage, as specified in Ontario Regulation 188/08, s. 45 (1).

FSCO found no violations in the last three years, indicating general industry compliance as a result of brokerage enhancement of policies and procedures.

Figure 9 – Compliance with Payments of Incentives Other Than Money

Year	2010	2011	2012	2013	2014
Risk Rating					

9. Required Records

Within this section FSCO verified whether mortgage brokerages meet all the requirements regarding the maintenance of records as specified in Ontario Regulation 188/08, s. 46.

Upon review of policies and procedures, FSCO noted an increase in compliance year-over-year, signifying an improvement in the maintenance of required records.

Figure 10 – Compliance with Maintenance of Required Records

Year	2010	2011	2012	2013	2014
Risk Rating					

10. Security of Records

FSCO verified whether mortgage brokerages maintain all records securely, and have taken sufficient precautions to guard against falsification of records as prescribed in Ontario Regulation 188/08, s. 47.

FSCO observed a consistently high level of compliance with this section.

Figure 11 – Compliance with Secure Maintenance of Records

Year	2010	2011	2012	2013	2014
Risk Rating					

11. Records Retention

This section refers to Ontario Regulation 188/08, s. 48, and within it FSCO verified whether mortgage brokerages retained all required records for the minimum amount of time and in an approved location as prescribed under the statute.

FSCO observed an upswing of compliance in 2013 and 2014.

Figure 12 – Compliance with Records Retention

Year	2010	2011	2012	2013	2014
Risk Rating					

12. Trust Bank Account

This section was added to the examination program in 2012, referring to Ontario Regulation 188/08, s. 49-55. Since that date FSCO has reviewed whether mortgage brokerages holding trust funds have established adequate policies and procedures regarding: the brokerage obtaining written consent from FSCO if they opened more than one trust bank account; maintenance of the designated trust bank account; preparation of monthly bank reconciliations; and, immediate notification to FSCO if there is a shortfall in the trust bank account.

FSCO observed there to be very few violations by the mortgage brokerages with respect to this section.

Figure 13 – Compliance with Trust Bank Account Requirements

Year	2010	2011	2012	2013	2014
Risk Rating	N/A	N/A			

13. Other Matters

The questions in this section relate to the use of the premises where the mortgage brokerage is located, and the use of client personal information when conducting business, per Ontario Regulation 188/08, s. 56, 57.

FSCO identified a high rate of compliance in the most recent three years.

Figure 14 – Compliance with Other Matters

Year	2010	2011	2012	2013	2014
Risk Rating					

Conclusion

Based on FSCO's assessment of examinations conducted during the period from 2010 to 2014, the overall results have demonstrated that in general, the majority of mortgage brokerages understand the requirements of the MBLAA, and FSCO's expectations for brokerages to have complete policies and procedures to govern their day-to-day activities and ensure compliance with the legislation.

In general, policies and procedures appear to be adequate for the nature, complexity and size of the mortgage brokerages examined. However, FSCO's findings reveal an unacceptable decline in the level of compliance regarding public relations materials and disclosure requirements.

Going forward, FSCO will be assessing regulatory responses to correct for these specific contraventions. Brokerages need to review, refine and adjust their internal controls on an ongoing basis to ensure continuing compliance with the law.

Over the past five years, FSCO has issued 83 AMPs as a result of identified violations arising from compliance reviews, including brokerage examinations. In the majority of these cases, FSCO found that brokerages failed to demonstrate compliance with standards of practice regulations, including disclosure requirements, and insufficient and/or lacking required policies and procedures. The AMPs imposed ranged from \$250 to \$25,000. To learn more about these cases and other FSCO enforcement activities go to: [Enforcement Online](#).

FSCO will continue to conduct on-site brokerage examinations to assess the industry's level of compliance with the law. Brokerages should take reasonable steps to ensure that their policies and procedures and internal controls are adequate to achieve compliance with the legislated practice standards. For more information go to [Checklists for the Mortgage Brokering Industry](#).

As regulations are amended and as business practices change, FSCO will adjust its examination programs to incorporate new regulatory requirements and to account for the need to ensure borrowers, investors and lenders are treated fairly.