

MORTGAGE COLLECTIONS IN BRITISH COLUMBIA

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WHAT IS A MORTGAGE?

A mortgage is “a conveyance of property as a security for the payment of a debt or the discharge of some other obligation for which it is given, the security being redeemable on the payment or discharge of such debt or obligation.”¹ So a mortgage is comprised of two parts:

- (a) a promise to satisfy an obligation (usually; pay a debt) (a “Covenant”); and
- (b) a conveyance of property² as security for the Covenant (a “Charge”).

WHAT DOES A MORTGAGE CHARGE?

Although mortgages most commonly charge only real property (land), the Charge can be over any type of property; real property, personal property, incorporeal property or any combination of those. Mortgages of real property are exactly that; the Charge gives the lender as security for the Covenant an interest in the real property charged and buildings and fixtures (which at law are treated as part of the real property), and nothing more.

Relatively few mortgages of real property are of bare land; most involve real property in conjunction with buildings, fixtures, personal property and (occasionally) incorporeal property. Mortgages of residential real property almost always involve real property in conjunction with buildings and personal property (e.g. appliances, lighting “fixtures,” window coverings, air conditioners, vacuum systems, etc.) and not infrequently incorporeal property (e.g. rents). Mortgages of commercial real property almost always involve real property in conjunction with buildings, personal property (e.g. the personal property described above plus inventory, equipment, machinery, supplies, etc.) and often incorporeal property (e.g. liquor and other government licenses, protected business names, contracts with suppliers and builders, etc.).

Some lenders attempt to increase the scope of their security by taking assignments of rents (perhaps more properly; mortgages of personal property) and/or security agreements (mortgages of personal property) as collateral security for loans secured primarily by mortgages of real property. Assignments of rents are commonplace and only involve a few enforcement considerations.

Collateral security agreements, however, present their own fairly complex security and enforcement considerations, which are beyond the scope of this paper.³ In addition, loans often do not secure incorporeal property.

WHAT RIGHTS DOES A MORTGAGE LENDER HAVE?

From a lender’s perspective, a mortgage is essentially security for money lent. Lenders have rights against the parties to the Covenant (rights “against the person” or “*in personam*”) and they

¹ 21 Halsbury, Laws of England, 1st ed. (1912), p.70

² Or, arguably, now only a charge on property as a result of section 25 of the Land Title Amendment Act, S.B.C. 1989, ch. 69

³ See, for example, Foreclosures, Debentures and Bankruptcy for Legal Assistants, BC Continuing Legal Education, June, 1985. The problems related to “seize or sue” have been changed, but not eliminated, by the Personal Property Security Act, S.B.C. 1989, ch. 36

have rights against the property which is the subject of the Charge (rights “against the property” or “*in rem*”).

IN PERSONAM

There is one principal legal remedy for lenders enforcing rights *in personam*; they are enforced through the Court by judgment. Covenants are then merged in judgments and lenders have the (often unsatisfactory) methods of enforcing (or “executing on”) judgments available to any other successful litigant. Exigible property of the parties to the Covenant (then “judgment debtors”) may be sold, by the Court Bailiff or otherwise (if any such property can be found). And Orders of the Court may be obtained requiring judgment debtors to make payments in satisfaction of judgments (although such Orders are often ignored by judgment debtors).

IN REM

There are two remedies for lenders enforcing rights *in rem*; sale and foreclosure.

SALE

By far the most common method of enforcing rights *in rem* is by sale through the Court. Ownership of real property is fairly certain and simple, due to the Torrens land title system in British Columbia. Real property cannot be moved out of the jurisdiction or otherwise hidden. And there is always a reasonably active market for real property.

Mortgages often still provide that lenders with a mortgage in default can sell the property which is the subject of the Charge without the assistance of the Court.

That is the single most common and powerful remedy available to lenders in some jurisdictions, including Ontario. But it is very doubtful if the land title offices in British Columbia would participate in such sales, thereby making them of little or no value. And the British Columbia Court of Appeal has made it clear that lenders attempting to sell real property privately under the terms of their mortgages will be faced with the same delays as lenders doing so in the normal way through the Court.⁴ As a practical matter, all lenders in B.C. sell their mortgaged real property under the Rules of Court and in foreclosure proceedings (“Foreclosures”). Doing so generally protects lenders (absent bad faith) from actions against them in wrongful sale (which are fairly common in Ontario and other jurisdictions that allow private or “extra-judicial” sales) and the process is common and well understood by realtors, the land title offices and others.

FORECLOSURE

This is the “original” method of enforcing mortgages. Lenders can obtain from the Court in a Foreclosure an Order (an “Order Absolute”) which has the effect of extinguishing all rights of the borrower and all parties with interests in the real property which is the subject of the Charge ranking subsequent to the lender (“subsequent chargeholders”). An Order Absolute makes the lender the legal and beneficial owner of the real property and vests title to the real property in the lender free of all charges except those of parties

⁴ SouthWest Marine Estates Ltd. v. Bank of B.C. (1985), 65 B.C.L.R. 328 (B.C.C.A.)

with interests in the real property ranking prior to the lender (for example, property taxes, most condominium charges, etc.). The lender can register an Order Absolute at the land title office, which will create a new title to reflect the foregoing. An Order Absolute requires all parties in possession of the real property to deliver up possession to the lender, failing which they can be evicted by the Court Bailiff or Sheriff. Orders Absolute are treated as conveyances for the purposes of the *Property Purchase Tax Act*⁵ and, like any transfer of real property in British Columbia, subject the purchaser (in this case, the lender) to tax (calculated at 1% on the first \$200,000 of the fair market value of the real property and 2% of the balance). Orders Absolute also have the effect under Section 28 of the *Property Law Act*⁶ of making all judgments or covenants unenforceable. Orders Absolute are relatively rare as a result of the requirement to pay property purchase tax and their making judgments unenforceable.

HOW ARE A MORTGAGE LENDER'S RIGHTS ENFORCED?

A Foreclosure is the judicial summary proceeding by which a lender enforces a mortgage in British Columbia. It is enforcement of the Covenant (by judgment and execution) and enforcement of the Charge (by sale or foreclosure). Very simply stated, Foreclosures usually proceed as follows (see Schedule "A"):

DEFAULT

A borrower defaults under the terms of a mortgage. Default commonly consists of default in periodic payments but can also consist of maturity of a mortgage, default in payment of taxes, condominium charges, or breach of other terms and conditions in a mortgage.

DEMANDS FOR PAYMENT

Demand is made on all parties liable on the Covenant. The demand accelerates the mortgage balance if necessary (acceleration is not necessary if the mortgage has matured), provides a reasonable deadline for payment of the mortgage balance⁷ and indicates a Foreclosure may be commenced after the demand period expires.

PREPAYMENT PENALTY

Once the mortgage is accelerated, the lender waives any right it has to a prepayment penalty or bonus.⁸

⁵ R.S.B.C. 1987, ch. 15

⁶ R.S.B.C. 1979, ch. 340

⁷ see *Lister v. Dunlop et. al.*, [1982] 1 S.C.R. 726 and section 244 of the *Canada Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (establishing the now almost universal 10-day demand period)

⁸ section 8 of the *Canada Interest Act*, R.S.C. 1935, c.I-15

COMMENCEMENT

After the demand period expires, a search of the real property is conducted at the appropriate land title office and the following three documents necessary to commence a Foreclosure are drafted;

- (a) a Petition;
- (b) an Affidavit supporting the facts in the Petition;
- (c) a certificate of pending litigation (a “CPL”).

The Petition and the CPL are finalized and executed. The Affidavit is finalized and sworn. The Petition, Affidavit and CPL are all filed at the appropriate Court registry and the CPL is immediately thereafter filed at the appropriate land title office.

PARTIES

The Petition names as parties to the Foreclosure all parties liable on the Covenant and all subsequent chargeholders (for example, second mortgageholders, judgment creditors and builders’ lien claimants).

PERSONAL SERVICE

After the CPL is filed at the land title office, a search is conducted of the real property to ensure that all subsequent chargeholders are named in the Foreclosure. Then all parties to the Foreclosure must be served.

Parties served within Canada have 21 days to file a Response to Petition (a document wherein the party admits service, attorns to the jurisdiction of the Court, provides an address for delivery of further documents, and provides details of any opposition to the relief sought in the Petition). Parties served in the United States have 35 days; and parties served outside Canada and the United States have 49 days.

When filing a Response to Petition, a party that is opposing any of the relief sought in the Petition must also file any Affidavit(s) supporting such opposition.

ALTERNATIVE SERVICE

Sometimes parties are impossible to locate, or intentionally evade personal service. In that event, an Affidavit is obtained from a process server setting forth the attempts to locate and/or serve the party and explaining that it is impractical to effect personal service. Often, skip trace reports are also obtained. An *ex parte* application is made to the Court for an Order allowing the lender to effect alternative service on that party. Methods of alternative service include service on a related party such as a spouse, posting a notice at the party’s residence, emailing and/or mailing to the party, and publication of a notice in a local newspaper.

HEARING OF PETITION

Once all parties to a Foreclosure have been served (personally or by substituted service) and once the time for filing Responses to Petition by all parties has elapsed a search is conducted in the Court Registry for Responses to Petition, and a Notice of Hearing of Petition is filed, naming a Court date at least 8 business days after its filing. Copies of the Notice of Hearing of Petition are delivered to all parties who have filed a Response to Petition at the addresses specified in their Responses to Petition, and mailed to all other parties at the addresses at which they were served.

RELIEF AGAINST ACCELERATION

If the mortgage has not matured, a borrower can apply to the Court under section 21.1 of the *Law and Equity Act*⁹ for “relief against acceleration.” Normally, the Court will allow the borrower to reinstate his mortgage by paying all missed payments, interest, taxes, insurance, condominium charges and the lender’s legal expenses. Applications for such Orders are rare because lenders generally allow reinstatement on those terms, without the necessity of a Court Order.

DEFENCE

A borrower can swear and file an Affidavit setting forth facts giving rise to a defence and then apply to the Court for an Order transferring the Foreclosure to the trial list. Such Orders are relatively rare as there is seldom a *bona fide* triable issue in a Foreclosure. If there is, and if an Order is made transferring the Foreclosure to the trial list, the lender is faced with the very significant expense and delay of a civil trial.

ORDER NISI

Barring a successful application for relief against acceleration or a transfer of the Foreclosure to the trial list, the lender applies to the Court for Order Nisi. This is, in many ways, the most important Order in a Foreclosure. There are four main components to an Order Nisi;

- (a) a declaration that the mortgage is in default and an Order setting the redemption period (the time during which, prima facie, the mortgage may be paid out or “redeemed”);
- (b) a summary accounting of the amount owing under the mortgage as of the date of Order Nisi;
- (c) judgment against all parties liable on the Covenant, in the amount of the mortgage debt as of the date of Order Nisi;
- (d) costs.

⁹ R.S.B.C. 1979, ch. 224

REDEMPTION PERIOD

Normally, the redemption period is set at 6 months. The redemption period can be shortened or eliminated¹⁰ if the lender can show some or all of the following:

- (a) the net sale proceeds of the real property after payment of taxes, commission, etc. would clearly be less than the mortgage debt;
- (b) abandonment of the real property.

SUMMARY ACCOUNTING

The summary accounting is established from the mortgage accounts in the Petition, which are sworn to by a representative of the lender in an Affidavit. The provision in the Order Nisi for a summary accounting also allows the lender to re-apply for a further summary accounting in the event further monies are properly spent under the mortgage by the lender during the redemption period (for example, for payment of property taxes, insurance, etc.).¹¹

ORDER FOR CONDUCT OF SALE DURING THE REDEMPTION PERIOD

Any subsequent chargeholder is in jeopardy of having its interest in the real property foreclosed by Order Absolute after the expiration of the redemption period. Accordingly, any subsequent chargeholder is entitled to apply for an Order for Conduct of Sale during the redemption period, to protect itself from being foreclosed. An Order for Conduct of Sale allows a subsequent chargeholder to list the real property for sale with the realtor of its choice, to show the real property to realtors, appraisers and prospective purchasers at reasonable times, and to post signs indicating the real property is for sale. The subsequent chargeholder obtaining an Order for Conduct of Sale generally obtains an appraisal and lists the real property for sale (at least initially) at a price slightly above the appraised value.

EXTENSIONS OF THE REDEMPTION PERIOD

Covenantors and subsequent chargeholders can apply for one or more Orders extending the redemption period. To obtain such an Order, the applicant must satisfy the Court (by current appraisal evidence) that¹²:

- (a) there is sufficient equity in the real property to protect the lender during the extended redemption period; and
- (b) there is a reasonable prospect of the mortgage being paid out during the extended redemption period (usually by sale or refinancing of the real property).

¹⁰ For an analysis of the principles governing shortening redemption periods, see CIBC Mortgage Corporation v. Burnham (1986) 2 B.C.L.R. (2d) 130 (B.C.S.C.)

¹¹ The extent of the further summary accounting is not simple. See, for example, Eaton Bay Trust Company v. Innerspace Developments Ltd. et al. (1987), 10 B.C.L.R. 29 (B.C.S.C.) or CIBC v. Duguay, unreported, Vancouver Registry number H890500

¹² Canada Permanent Mortgage Corporation v. Dan-Al Construction Co. Ltd., B.C.C.A., Vancouver Registry CA820313

Extensions of redemption periods are generally for three months.

LENDER'S REMEDIES AFTER THE REDEMPTION PERIOD

After the expiration of the redemption period (and any extensions), a lender has two choices:

- (a) it can apply for Order Absolute; or
- (b) it can apply for an Order for Conduct of Sale; such an Order will vacate any earlier Order for Conduct of Sale to a subsequent chargeholder.

APPROVAL OF SALE

Any party with an Order for Conduct of Sale (either a subsequent chargeholder during a redemption period or a foreclosing lender after the expiration of a redemption period or (rarely) for that matter another party to the Foreclosure) can accept an offer to purchase the real property, subject only to Court approval. Thereafter, the party accepting the offer can apply to the Court for an Order approving its sale. These applications are often opposed, and the questions of fair market value and proper marketing are often argued at length, and determinative.

COMPLETION OF SALE

The party obtaining the Order approving a sale has the responsibility of completing the sale¹³ and the net sale proceeds are normally directed by the Order to be paid as follows:

- (a) taxes, utilities, condominium charges;
- (b) real estate commission;
- (c) lender's mortgage;
- (d) all subsequent chargeholders, in order of registration¹⁴;
- (e) any balance to the borrower or into Court.

DELAY IN SALE

Lenders attempting to enforce their rights *in rem* in mortgages by sale through Foreclosures are often faced with six-month redemption periods and three or even six month extensions of those redemption periods. Generally, lenders cannot obtain Orders for Conduct of Sale during the redemption periods established in their Foreclosures.¹⁵ This is so even for commercial real

¹³ And such parties should be aware of the risks inherent in doing so; for most if not all purposes they are treated as the vendor. See *Wiebe v. Rooke* (1985) 67 B.C.L.R. 257 (B.C.C.C.)

¹⁴ *Roadburg v. Cedarhurst*, sub nom *Roadburg v. R. in Right of British Columbia* (1981), 21 B.C.L.R. 114, (B.C.C.A.)

¹⁵ *Pope v. Roberts* (1979) 10 B.C.L.R. 50 (B.C.C.A.)

property and is often frustrating for lenders; they are faced with lengthy delays in enforcement by sale, with the resulting interest accrual, market and other risks.

UNRECOVERABLE LOSS

Since the decision of *Canlan Investment Corporation v. Gibbons*¹⁶, the Court generally requires lenders to apply for judgment against all of the covenantors at the date of Order Nisi. The effect of merging the covenants to judgment at Order Nisi is to reduce the interest payable *in personam* by the parties to the Covenant thereafter to government prescribed post-judgment interest rates pursuant to section 7 of the *Court Order Interest Act*.¹⁷ Accordingly, from the date of Order Nisi on, the mortgage debt will increase at a different rate (the mortgage interest rate) than the judgment.¹⁸ Even if the judgment is obtained at a later date, the common practise of the Court is to award interest from the date of Order Nisi on at post-judgment interest rates.¹⁹

If the real property sells for a sufficiently high price, the lender will have its principal and mortgage interest completely repaid. If the real property does not sell for a sufficiently high price, the lender will apply all of the net sale proceeds to the judgment and retain its right to pursue the covenantors for any balance owing under the judgment plus legal costs. Because of the interest differential between mortgage debts and judgments described above, situations arise in which the net sale proceeds are sufficient to pay off judgments (leaving the lender with no remedy) but insufficient to pay off the mortgage debt (leaving the lender with an unrecoverable loss).

LOCAL VENUE

Since amendments to the *Law and Equity Act*²⁰ in 1986, mortgages must be foreclosed, simply stated, in the Supreme Court registry nearest the mortgaged real property. Section 18.3(2) provides that “Unless the Court otherwise orders, every foreclosure proceeding on a mortgage shall be commenced, where the real property ...is...in a municipality (with a Supreme Court registry) at that registry, or where the real property...is not...situated in a municipality...or...in a municipality...(without a Supreme Court registry) at any registry...in the judicial district in which the real property is situated...” There are approximately forty municipalities in British Columbia with Supreme Court registries and some of them have Court hearings as infrequently as once every one or two months. Mortgages of property in the Lower Mainland may be enforced in the Vancouver or New Westminster registries (which have Court hearings every day). Apart from that area, any enforcement of mortgages involves extra delay.

¹⁶ (1983), 42 B.C.L.R. 199 (B.C.S.C.)

¹⁷ 17 R.S.B.C. 1979, ch. 76

¹⁸ There has been some confusion in the authorities as to this proposition. That presumably ended in the decision of the *Court of Appeal in Courtenay Savings Credit Union v. Harle* (1987), 13 B.C.L.R. (2d) 357 (B.C.C.A.). See also *Norfolk Trust v. Wolcoski* (1982), 38, B.C.L.R. 130 (B.C.C.A.), *Canada Permanent Trust Company v. Nykodym* (1983) 50 B.C.L.R. 18 (S.C.) and *Bank of Montréal v. Spence* (1984), 58 B.C.L.R. 343 (S.C.) *Bank of British Columbia v. Ballance*, [1983] 2 W.W.R. 566 (B.C.S.C.) (contra) now appears to be bad law.

¹⁹ *Crown Trust Company v. M.J. Hall & Associates Ltd.* (1984), 50 B.C.L.R. 11 (B.C.S.C.)

²⁰ *infra*

SCHEDULE "A"

