

FINANCIAL SERVICES TRIBUNAL

IN THE MATTER OF the *Mortgage Brokerages, Lenders and Administrators Act, 2006*, S.O. 2006, c. 29 (the “Act”), in particular sections 7, 18, 19, 21, 29, 38 and 39, and the following Regulations under the Act; the Mortgage Brokerages: Standards of Practice Regulation, O. Reg. 188/08, in particular s. 42, and the Administrative Penalties Regulation, O. Reg. 192/08, in particular, section 3;

AND IN THE MATTER OF Mortgage Magician Inc.;

AND IN THE MATTER OF a request for hearing pursuant to subsection 39(5) of the Act.

BETWEEN:

MORTGAGE MAGICIAN INC.

Applicant

-and-

SUPERINTENDENT OF FINANCIAL SERVICES

Respondent

BEFORE:

Mr. Colin McNairn
Member of the Tribunal and Chair of the Panel

Mr. Martin Brown
Member of the Tribunal and of the Panel

Mr. Ralph Scane
Member of the Tribunal and of the Panel

APPEARANCES:

Mr. Marshall Godfrey, president and principal broker for Mortgage Magician Inc., representing the applicant Mortgage Magician Inc.

Mr. Stephen Scharbach, counsel, representing the respondent, the Superintendent of Financial Services

HEARD:

May 29, 2009

REASONS FOR DECISION

A. Background and Relevant Facts

The Superintendent of Financial Services (the “Superintendent”), the chief executive officer of the Financial Services Commission of Ontario (“FSCO”), is authorized to issue mortgage brokerage licences under the terms of the *Mortgage Brokerages, Lenders and Administrators Act, 2006*, S.O. 2006, c. 29 (the “Act”, sometimes called the “*MBLAA*”), which came into force on July 1, 2008.

Mortgage Magician Inc. (“MMI”) applied for a mortgage brokerage licence under the Act. The application form contained a section that read as follows:

12. Errors and Omissions Insurance: (check applicable box)

The corporation/partnership/sole proprietor, currently has the required errors and omissions insurance in place. Note: if using an existing policy the applicant must have extended coverage for fraudulent acts in place.

or

The corporation/partnership/sole proprietor, will have by July 1, 2008, the required errors and omissions insurance in place.

Note: Only applicants with the required errors and omissions insurance are licensed on July 1, 2008.

In the application form as completed and signed on behalf of MMI by its president Mr. Marshall Godfrey (the “Application”), the second box in the errors and omissions

insurance section appears to have been checked but that check appears to have been crossed out. There is no marking at all in the first box in the errors and omissions insurance section of the Application. As a result of the Application, MMI was granted a mortgage brokerage licence on April 15, 2008, to be effective on July 1, 2008. It appears that the Superintendent took the crossed-out checkmark on the Application as a statement that errors and omissions insurance would be in place by July 1, 2008 and issued the licence accordingly.

Mortgage brokerages are required by section 42 of the Mortgage Brokerages: Standards of Practice Regulation to maintain E&O insurance in a form approved by the Superintendent and with a minimum level of coverage (“E&O insurance”). This Regulation was not in effect at the time MMI applied for a mortgage brokerage licence or at the time it was granted such a licence. It did, however, come into effect on July 1, 2008, with the result that the requirement applied at the time MMI’s mortgage brokerage licence became effective and thereafter. Beginning well before July 1, 2008, FSCO undertook an extensive communications program to alert the mortgage brokerage community to the requirements under the Act, including the proposed E&O insurance requirement.

On November 26, 2008, FSCO sent an urgent e-mail to MMI to the attention of its principal broker;

- stating that the principal broker was responsible for ensuring that his mortgage brokerage complies with every requirement of the Act,
- advising that the mortgage brokerage was found, as a result of an audit, to have failed to obtain E&O insurance as of October 15, 2008,
- emphasizing the importance of the requirement, in the regulations under the Act, to have E&O insurance and that a failure to obtain such insurance could lead to enforcement action including an administrative penalty and revocation of licence,
- noting that the only acceptable insurance was specific E&O mortgage broker insurance secured from one of five FSCO –approved insurance providers, and
- requiring an e-mail response no later than December 3, 2008, such response to include a detailed description of why E&O insurance was not in place, supporting documentation including any insurance policy/declaration page and a statement of the amount of business conducted since July 1, 2008.

This e-mail also included a series of additional questions and answers (“Q and A’s”). The first Q and A was as follows:

Q: I have not done any business under the *MBLAA* and/or got my licence just in case I wanted to do business in the future. Do I still need coverage and am I still in violation of the *MBLAA*?

A: Yes you still require coverage and are in violation of the *MBLAA*.

Mr. Godfrey sent an e-mail to FSCO later the same day, stating that;

- he had an unblemished record as a mortgage broker for over 20 years and had never carried errors and omissions insurance, and
- business was slow and he couldn't afford insurance coverage, noting that he hadn't processed a mortgage deal since June 2008.

He then expressed the hope that FSCO would be able to help resolve his situation.

FSCO did not respond to Mr. Godfrey's e-mail of November 26, 2008, but a FSCO staff member attempted to reach MMI by phone on February 9, 2009 at the phone number for the mortgage brokerage that appeared on the Application and left a voice message. No one returned the call. The contents of the voice message were not disclosed at the hearing, so we are not aware of what was requested of Mr. Godfrey.

On March 6, 2009, the Superintendent served MMI with a notice of proposal to revoke its mortgage brokerage licence, a notice of proposal to impose an administrative penalty in the amount of \$1,000 and an interim order suspending the licence, each of which included supporting reasons. On March 10, this Tribunal received a request for a hearing from MMI, which was apparently in respect of both of the notices of proposal served by the Superintendent on MMI.

On March 21, 2009, MMI provided FSCO with satisfactory proof that it had arranged for E&O insurance, which was in place as of March 9, 2009.

At the beginning of the hearing in this matter, the parties advised the Tribunal that MMI was withdrawing its request for a hearing in respect of the notice of proposal to revoke its mortgage brokerage licence as the Superintendent had agreed not to proceed with the revocation of the licence, as proposed in the notice of proposal with its supporting reasons, and had agreed to cancel the interim suspension of the licence, in light of the fact that MMI had now arranged for E&O insurance.

B. Issue

The remaining issues to be determined in this case are as follows:

1. Is the imposition of an administrative penalty against MMI justified in the circumstances of this case, and
2. If so, what should be the amount of that penalty in those circumstances.

C. Analysis

1. Whether an Administrative Penalty against MMI is Justified

Mr. Godfrey admitted, in his evidence before the Tribunal, that MMI was available to carry out mortgage brokerage activities after July 1, 2008. Indeed, MMI continued to maintain a listing after that date in the yellow pages of the local telephone directory. He maintained, however, that if someone had come to him to process a mortgage deal during that period, MMI would have obtained the required E&O insurance before he acted on the matter. He said that he understood that such insurance was not necessary so long as the authority conferred by a mortgage brokerage licence, to process mortgage deals, was not actually being used.

Subsection 39(1) of the Act provides that if the Superintendent is satisfied that a person has failed to comply with a requirement established under the Act, he may, by order, impose an administrative penalty on that person. If a hearing is requested, in respect of a proposal by the Superintendent to make such an order, the Tribunal must be satisfied that there has been such a failure to comply before confirming the proposal and directing the Superintendent to carry it out. In the present case, counsel for the Superintendent argued that there were two requirements established under the Act with which MMI had failed to comply, namely;

- (a) the requirement, under section 42 of the Mortgage Brokerages: Standards of Practice Regulation, that mortgage brokerages maintain E&O insurance, which is a prescribed standard of practice with which licensed mortgage brokerages are required to comply under the terms of subsection 7(4) of the Act, and
- (b) the requirement, under subsection 29(2) of the Act, that licensees shall give the Superintendent such information and documents as the Superintendent may request and do so in the manner and within the period specified by the Superintendent.

Superintendent's counsel maintained that MMI did not comply with the second requirement as it failed to provide the information and documents requested by FSCO, acting on behalf of the Superintendent, in its e-mail of November 26, 2008 that was addressed to the attention of MMI's principal broker.

(a) Failure to Comply with the Requirement to Maintain E&O Insurance

We are satisfied that MMI failed to comply with the requirement, established under the Act, to maintain E&O insurance. That failure continued for the period from July 1, 2008 until March 6, 2009, when MMI's mortgage brokerage licence was suspended by order of the Superintendent, only then eliminating the necessity for E&O insurance. Therefore, we have the discretion to impose an administrative penalty upon MMI on the basis of its failure to maintain E&O insurance. The fact that MMI ultimately obtained E&O

insurance, with effect from March 9, 2009, does not remedy the failure to maintain such insurance during the period from July 1, 2008 to March 6, 2009.

Mr. Godfrey's apparent misunderstanding to the effect that MMI didn't have to maintain E&O insurance so long as it didn't process any mortgage deals is not a sufficient reason for declining to exercise our discretion to impose an administrative penalty. His understanding was certainly unreasonable after November 26, 2008, if not before. On that date, he received FSCO's e-mail seeking an explanation for MMI's lack of E&O insurance and including a Q and A that made it abundantly clear that such insurance was required even if no business was, in fact, being done under a mortgage brokerage licence. In his e-mail to FSCO of the same date, Mr. Godfrey effectively acknowledged receipt of FSCO's e-mail. However, in his evidence before this Tribunal, Mr. Godfrey maintained that he never saw the Q and A and didn't believe it was in the e-mail he received from FSCO. Ms. Yen Quan Low Sin, Senior Registration Specialist with FSCO, testified that the Q and A's were part of FSCO's four page e-mail of November 26, 2008 that was sent to all mortgage brokerages shown by a FSCO audit to be without E&O insurance, which would have included MMI. On the basis of this oral evidence and a copy of what purports to be an e-mail of November 26, 2008 from FSCO to MMI that was admitted in evidence in this proceeding on the consent of the parties, we have concluded that the Q and A's were part of the November 26 e-mail that FSCO sent to MMI.

In conclusion, we believe that, in the circumstances, the imposition of an administrative penalty against MMI is justified on the basis of MMI's failure to maintain E&O insurance. This is sufficient to dispose of the first issue in this case. However, we will go on to consider the Superintendent's alternative argument that the imposition of an administrative penalty against MMI is also justified on the basis of a failure by MMI to comply with the requests for information and documents in FSCO's e-mail to MMI of November 26, 2008.

(b) Failure to Give the Superintendent Requested Information and Documents

In its e-mail of November 26, 2008 to MMI to the attention of its principal broker, FSCO asked, presumably on behalf of the Superintendent, for three items of information and documentation. The first item was a detailed explanation as to why MMI did not have E&O insurance. Mr. Godfrey responded to this request, in his e-mail to FSCO of the same date, by stating, in effect, that he had never carried insurance before and couldn't afford to now, business being so slow. This response may have been lacking in detail but it was largely responsive to FSCO's request.

The second requested item was supporting documentation including any insurance policy/declaration page. At this time, there was no insurance policy, and therefore no declaration page of such a policy, for MMI to provide. It is hard to imagine just what documentation might have been supplied to support Mr. Godfrey's explanation for why MMI didn't have E&O insurance. His explanation really speaks for itself. There was nothing in the evidence or argument before the Tribunal that would suggest precisely what supporting documentation could and should have been provided. Mr. Godfrey might

have attempted to get a written quote or quotes on the cost of obtaining E&O insurance from one or more of FSCO's approved insurance providers. However, FSCO must already have been aware of the approximate premium rates that would be charged by its approved providers. The written evidence of Mr. Grant Swanson, the Executive Director, Licensing and Market Conduct, of FSCO, which was admitted by the Tribunal on the consent of the parties, contains a statement to the effect that the financial benefit of avoiding the cost of insurance ranges in the amount of \$800 to \$1,200 per annum.

The last item requested of MMI was a statement of the amount of business the brokerage had conducted in terms of dollar volume and number of transactions since July 1, 2008. In his e-mail of November 26, 2008, Mr. Godfrey gave a complete response to this request by stating that MMI had conducted no such business.

Overall, Mr. Godfrey's responses to the various requests FSCO made to MMI in its November 26 e-mail were, in our view, responsive or substantially responsive to those requests and as complete as could be reasonably expected in the circumstances.

Mr. Godfrey also expressed the hope, in his e-mail of November 26, 2008, that FSCO might be able to help resolve his situation. FSCO did not respond to that e-mail and gave no indication to MMI that it was not satisfied with Mr. Godfrey's response to its request for information and documents nor did it advise MMI of what more, if anything, it needed from MMI.

In conclusion, we believe that, in the circumstances, the imposition of an administrative penalty against MMI is not justified on the basis of a failure by MMI to give the Superintendent such information and documents as were requested in FSCO's e-mail of November 26, 2008.

(c) The Permitted Purposes for the Imposition of an Administrative Penalty

Subsection 38(1) of the Act provides that an administrative penalty may be imposed for either of two purposes, namely to promote compliance with a requirement established under the Act and to prevent a person from deriving an economic benefit as a result of failing to comply with a requirement established under the Act. We have concluded that the imposition of an administrative penalty on MMI would satisfy both of these purposes (a similar conclusion was reached by the Tribunal in *Millennium Mortgage Corporation v. Superintendent of Financial Services* (FST Decision No. M0365-2009-1). Such a penalty would promote compliance by other persons with the requirements of the Act including, in particular, the requirement to maintain E&O insurance. It would also prevent MMI from realizing a modest economic benefit that MMI would otherwise enjoy, were it not offset by an administrative penalty, derived from its holding of a mortgage brokerage licence for the period from July 1, 2008 until March 6, 2009, while not having paid any premium for E&O insurance coverage during that period. We note that MMI continued to offer its mortgage brokerage services, at least through its yellow pages listing, during that period.

2. What Should be the Amount of the Administrative Penalty

In determining the appropriate amount of the penalty, we must take into account only those criteria set out in section 3 of the Administrative Penalties Regulation, just as the Superintendent was obliged to take into account those criteria in the first instance.

The first criterion is the degree to which the failure to comply with a requirement of the Act was intentional, reckless or negligent. It appears to us that Mr. Godfrey, acting on behalf of MMI, was negligent in the sense that he was seriously careless in not informing himself of the scope of the requirement, established under the Act, to maintain E&O insurance and in not obtaining that insurance before March of 2009.

The second criterion is the harm or potential harm to others resulting from the failure. There was no actual harm resulting from the failure of MMI to maintain E&O insurance during the period from July 1, 2008 to March 6, 2009 but, in our view, there was some potential for harm as a result of that failure. MMI was in a position, during that period, to process mortgage deals and may have done so without first obtaining E&O insurance, leaving its customers without the benefit of such insurance. The risk of that happening must, however, be tempered by the evidence of Mr. Godfrey, which we have no reason to doubt, to the effect that MMI would not have become involved in a mortgage deal without first taking out E&O insurance.

The third criterion is the extent to which the person tried to mitigate any loss or take any other remedial action. Mr. Godfrey did not take serious and timely action to remedy the failure of MMI to have E&O insurance in place on and after July 1, 2008 until March of 2009. The ultimate purchase of E&O insurance, with effect from March 9, 2009, did not remedy the lack of insurance during the period from July 1, 2008 until March 6, 2009.

The fourth criterion is the extent to which the person derived or reasonably might have expected to derive any economic benefit from the failure to comply with a requirement of the Act. As we have already concluded, MMI has received a modest economic benefit as a result of its failure to maintain E&O insurance.

The fifth criterion is any other contraventions or failures to comply with a requirement established under the Act or with any other financial services legislation, of Ontario or another jurisdiction, within the preceding five years. There was no suggestion that there was any such contravention or failure in this case.

Taking account of these criteria in their application to the circumstances of this case, we are of the opinion that an administrative penalty upon MMI of \$1,000 would be appropriate. This is not out of line with penalties imposed by this Tribunal in other similar cases (see *Millennium Mortgage Corporation v. Superintendent of Financial Services* (FST Decision No. M0365-2009-1) and *Airi v. Superintendent of Financial Services* (FST Decision No. M0353-2009-1)).

D. Order

For the foregoing reasons, we hereby direct the Superintendent, by order, to carry out his proposal to impose an administrative penalty upon MMI in the amount of \$1,000.

DATED at the City of Toronto, this 10th day of June, 2009.

“Colin McNairn”

Colin McNairn, Member of the Tribunal
and Chair of the Panel

“Martin Brown”

Martin Brown, Member of the Tribunal
and of the Panel

“Ralph Scane”

Ralph Scane, Member of the Tribunal
and of the Panel